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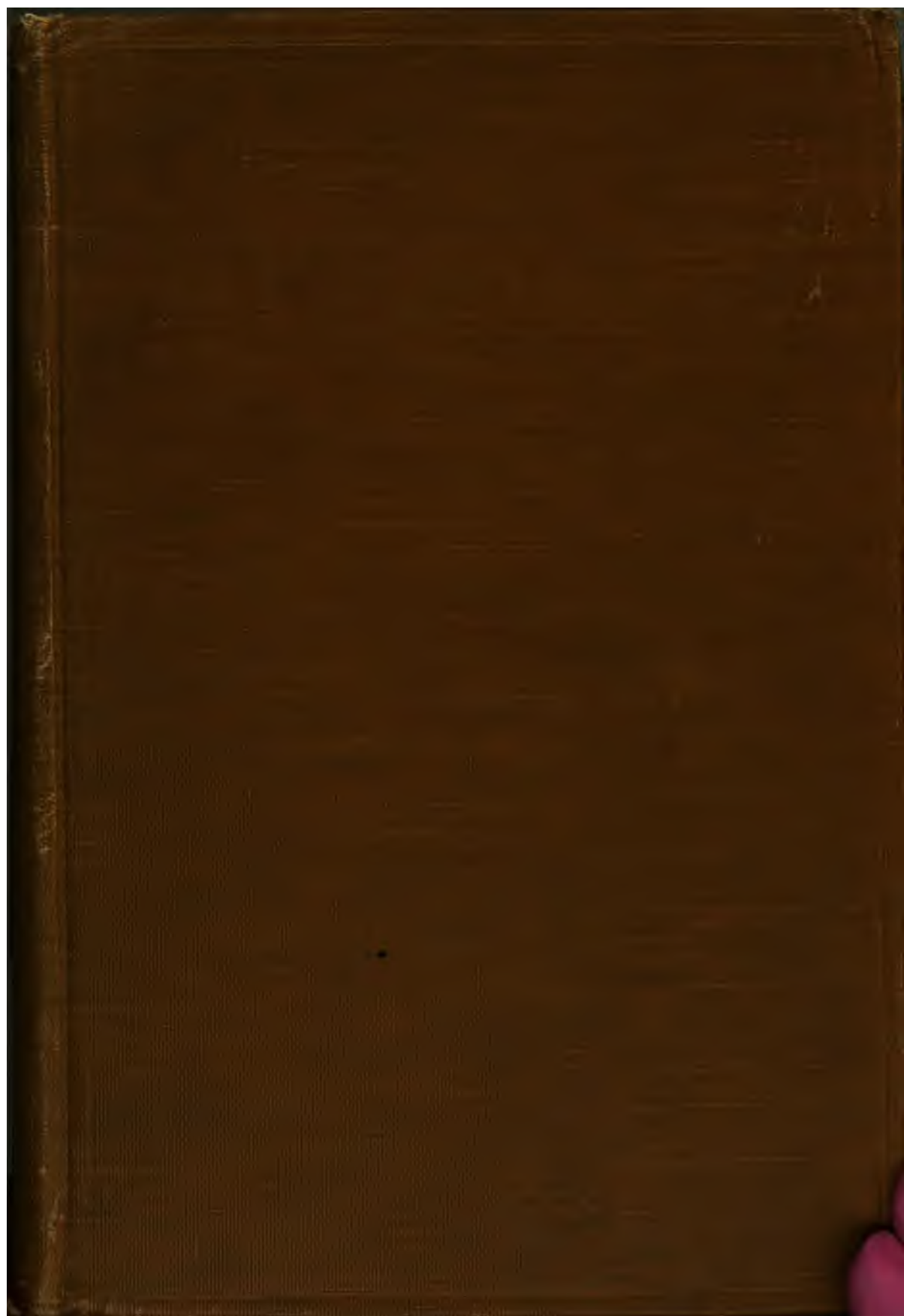
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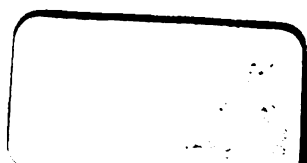
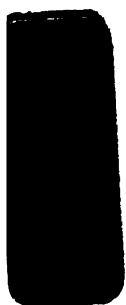
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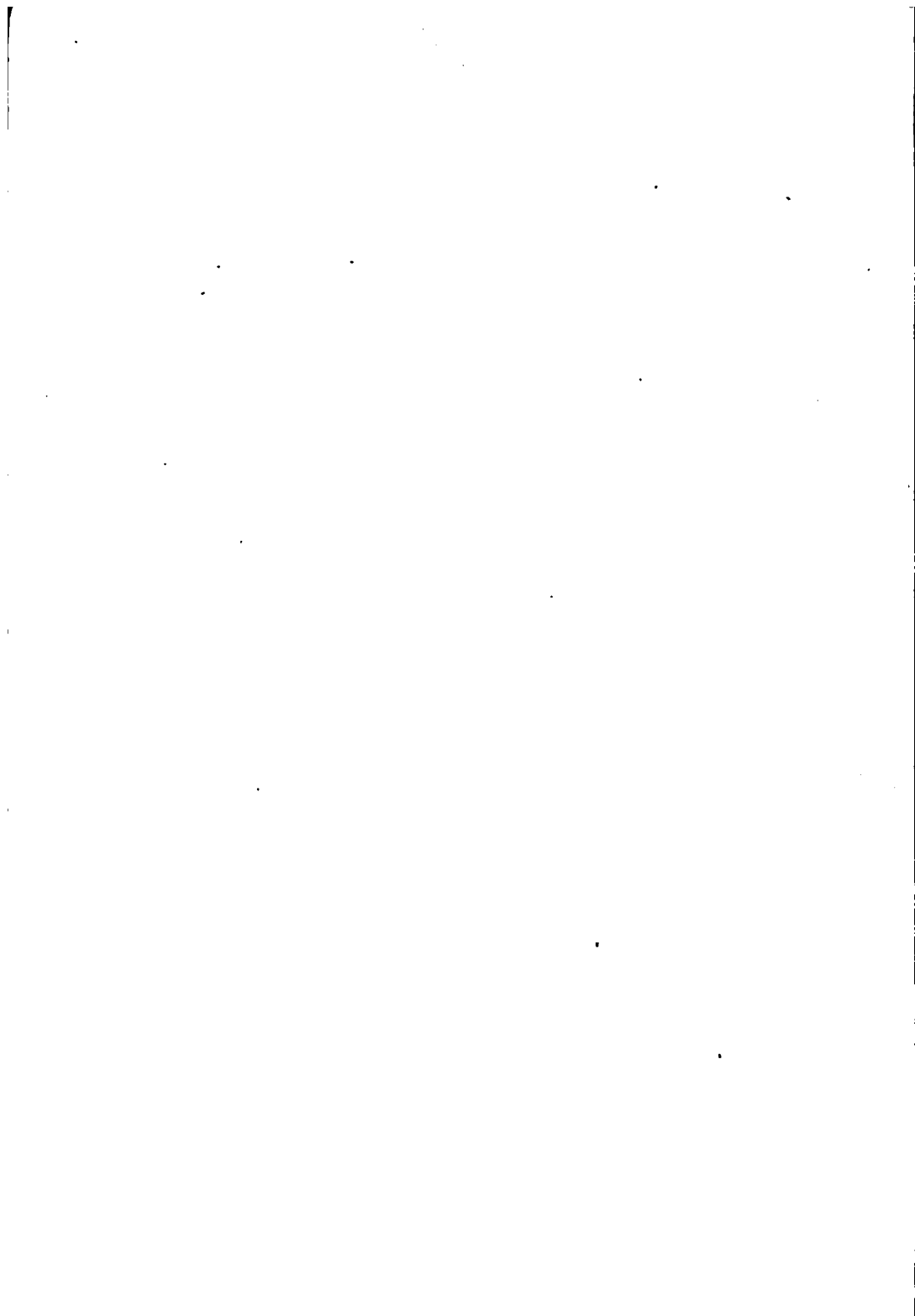
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Prof Edw. R. A. Seligman,
Columbia University.

Compliments of the
National Tax Association.

Allen Ripley Froto
President.

Columbus, Ohio.

March 10, 1908.

STATE AND LOCAL TAXATION



THE MACMILLAN COMPANY

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STATE AND LOCAL TAXATION

FIRST NATIONAL CONFERENCE

UNDER THE AUSPICES OF
THE NATIONAL TAX ASSOCIATION

COLUMBUS, OHIO

NOVEMBER 12-15, 1907

ADDRESSES AND PROCEEDINGS



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NATIONAL TAX ASSOCIATION

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*Secretary of New York Tax Reform Association, New York City
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INTRODUCTION

THE National Conference on State and Local Taxation was suggested in the spring of 1907 by Mr. Allen Ripley Foote, President of the National Tax Association. When sufficient progress had been made to warrant definite action, Mr. Foote submitted his plans and program to Hon. Andrew L. Harris, Governor of Ohio. Governor Harris was impressed with the importance of such a conference, and issued the following invitation to the Governors of the States:

"STATE OF OHIO
"EXECUTIVE DEPARTMENT
"OFFICE OF THE GOVERNOR

"COLUMBUS, August 20, 1907.

"GOVERNOR

"My dear Sir:

"I have the honor to request you to appoint three Commissioners to attend and represent your State in a National Conference for the consideration of the subject of State and Local Taxation, to be convened in Columbus, Ohio, November 12, 1907, under the auspices of the National Tax Association.

"The President of the Association, Mr. Allen R. Foote, has invited all Auditors or Comptrollers of State; all members of State Tax Commissions, Boards of Equalization and State Tax Commissioners; the Presidents and Professors of Economics and Public Finance of all Universities; and a large number of persons prominent in public and business affairs throughout the country, to attend and participate in the deliberations of this Conference.

"A list of subjects proposed for discussion and of persons who, up to date, have accepted invitations to prepare papers discussing specific branches of the subject, is submitted herewith. Other leaders of economic thought and experienced administrators of state and local tax laws will be added to the list of prepared papers from time to time, until all arrangements for the Conference are completed

INTRODUCTION

"The purposes of this Conference are:

"1. To secure an authoritative and an exhaustive discussion of the subject of state and local taxation in all of its details.

"2. To produce a volume of proceedings containing the best thought of those who, by reason of their special educational training and practical experience, are qualified to speak with authority upon the specific branch of the subject they may elect to discuss.

"3. To furnish to the members of the Legislatures of the several States a concrete, up-to-date statement of the economic and business principles that should be applied in state and local tax legislation, to be used as a guide for their action when considering proposals to improve the tax laws of their respective States and in the administration of the same.

"4. By this means to secure the application of correct economic and business principles in all tax legislation, and thus develop a high degree of uniformity in the tax laws of the several States.

"5. By securing uniformity in state tax laws, to eliminate the evil of changes in legal residence and in the location of business undertakings induced by differences in state tax laws, and to create conditions of high value in aid of the effective and economical management of the financial affairs of all state and local governments.

"Your consideration of and action upon this request at an early date is respectfully and earnestly desired.

"Kindly forward, at your earliest convenience, names and official or business address of the Commissioners you may be pleased to appoint to represent your State in this Conference.

"Assuring you of my high consideration, I am

"Very truly yours,

"ANDREW L. HARRIS,

"Governor of Ohio."

In response to this invitation, delegates representing thirty-three States and three Canadian Provinces attended the Conference, many of them being state or local tax officials. The presidents of universities were invited to send delegates, and thirty-one universities were represented. A number of local associations, interested in various phases of taxation, were represented by their officials.

Four Governors of States were present: Hon. Curtis Guild, Jr., Governor of Massachusetts, who presided; Hon. W. M. O. Dawson, Governor of West Virginia; Hon. Coe I. Crawford, Governor of South Dakota; and Hon. Andrew L. Harris, Governor of Ohio. There were also present Hon. A. C. Rutherford, Premier of Alberta, and Hon. A. J. Matheson, Treasurer of Ontario.

The Conference organized at Columbus, in the Board of Trade Auditorium, Tuesday afternoon, November 12, 1907, and closed Thursday evening, November 15, eight sessions being held. Speakers were limited to twenty minutes. In some cases, because of the absence of the speaker and the length of the program, papers were read by title upon recommendation of the program committee.

The meetings were open to the public, but voting was confined to the delegates.

The forty-eight papers presented to the Conference are published in this volume exactly as submitted by the writers. The Publication Committee deemed it best that the addresses be printed in full. However, as the volume is large, a number of purely formal remarks have been omitted from the report of the proceedings.

The resolutions adopted by the Conference were passed unanimously, with the exception of one to which there were three dissenting votes. They may be said, therefore, to represent fairly the views of both students of theories and practical administrators of tax laws.

As these resolutions propose certain changes in present state laws, it seems advisable, without going into detail, to say that there are now only six States whose constitutions permit these changes:

Connecticut, Delaware, New York, Pennsylvania, Rhode Island, Vermont.

In four States most, but not all, of the changes can be made without constitutional amendment:

Iowa, Minnesota, New Jersey, Oklahoma.

In every other State constitutional amendment, as recommended by the Conference, appears to be necessary. Practically none of these thirty-six States can grant any relief from the general property tax until constitutional limitations on the Legislature are modified or repealed.

It was the opinion of the members of the Conference that similar meetings should be held annually, and the details of the 1908 Conference will be arranged by the National Tax Association.

The Committee has had the assistance of Mr. Edward L. Heydecker, of New York, in the editing, proofreading, and indexing of this volume.

The Committee desire to express their appreciation, shared by all members of the Conference, of the earnest and efficient work of Mr. Allen Ripley Foote in making the preliminary arrangements for the Conference, in coöperating during its sessions, and in placing in the hands of this Committee a complete report of the proceedings.

A. C. PLEYDELL,
LAWSON PURDY,
JOHN H. MACCRACKEN,
Committee on Publication.

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RESOLUTIONS AND CONCLUSIONS ADOPTED BY THE CONFERENCE

INHERITANCE TAXATION

"Whereas, The several States are now taxing inheritances with marked success, and need all the revenue that can properly be drawn from this source; and

"Whereas, The federal government can readily raise additional revenue, when required, from other sources;

"Resolved, That it is the sense of this Conference that Inheritance Taxes should be reserved wholly for the use of the several States."

STATE CONSTITUTIONS

"Whereas, The greatest inequalities have arisen from laws designed to tax all the widely differing classes of property in the same way and such laws have been ineffective in the production of revenue; and

"Whereas, The appropriate taxation of various forms of property is rendered impossible by the restrictions upon the taxing power contained in the constitutions of many of the States;

"Resolved, That all state constitutions requiring the same taxation of all property, or otherwise imposing restraints upon the reasonable classification of property, should be amended by the repeal of such restrictive provisions."

INTERSTATE COMITY

"Whereas, The principles of international and interstate comity require that the same property should not be taxed by two jurisdictions at the same time, and the laws for the taxation of the transfer of property at death commonly transgress these principles; be it

"Resolved, That succession and inheritance tax laws should be so amended that the same property shall not be taxed by two jurisdictions at the death of the owner;

"Resolved, That the same principles should be applied in all tax legislation, to the end that no property should be taxed by two state jurisdictions at the same time; and

"Whereas, Retaliatory taxation is contrary to interstate comity and is in the nature of interstate war; be it

"Resolved, That all retaliatory legislation should be repealed."

PUBLIC DEBTS

"Whereas, The United States Supreme Court truly stated that a tax on public debts is a tax on the power of States, counties and municipalities to borrow money;

"Resolved, That the public debts of all States, counties and municipalities should everywhere be exempted from taxation."

HOME RULE

"Whereas, The reliance by state government for revenue upon the taxes ordinarily imposed on property as assessed by local officials has produced sectional injustice and jealousy and local inequality; and

"Whereas, The general property tax as a source of state revenue enforces a rigid uniformity which can take no account of actual conditions; be it

"Resolved, That state and local revenue systems should be so far divorced that by general laws the appropriate local governing bodies may, if deemed expedient, be granted certain limited and carefully prescribed powers over the licensing of occupations and the selection of subjects of local taxation and the rate of assessment upon such subjects."

OFFICERS OF THE CONFERENCE

Chairman

HON. CURTIS GUILD, JR.

Governor of Massachusetts

Vice-Chairmen

HON. WILLIAM M. O. DAWSON

Governor of West Virginia

HON. A. C. RUTHERFORD

Premier of Alberta, Canada

HON. WILLIAM O. THOMPSON

President of Ohio State University

Secretary

MRS. MARY C. SNYDER

Secretary of National Tax Association

FIRST SESSION

TUESDAY AFTERNOON, NOVEMBER 12, 1907, 2 TO 5 O'CLOCK

PROGRAM

1. CONFERENCE CALLED TO ORDER.
2. TEMPORARY CHAIRMAN.
3. ADDRESS OF WELCOME.
4. SECRETARY AND OFFICIAL STENOGRAPHER.
5. RESPONSE TO THE ADDRESS OF WELCOME.
6. PERMANENT CHAIRMAN.
7. VICE CHAIRMEN AND THEIR RESPONSES.
8. APPOINTMENT OF COMMITTEES:
 - (a) Program and Rules.
 - (b) Resolutions and Conclusions.
9. REPORT OF COMMITTEE ON PROGRAM AND RULES.
10. A COUNCIL OF STATES.

DR. CHARLES A. L. REED, University of Cincinnati,
Cincinnati, Ohio.

BOARD OF TRADE AUDITORIUM

COLUMBUS, OHIO, NOVEMBER 12, 1907

The first session of the National Conference on State and Local Taxation was called to order by Mr. Allen Ripley Foote, President of the National Tax Association, who spoke as follows:

MR. FOOTE:

As President of the National Tax Association, I now have the honor of calling to order this National Conference on State and Local Taxation.

This Conference has been organized for the purpose of bringing into touch those who represent the best economic thought and administrative experience on this subject throughout this country. The practical result sought is the formulation of a program of work that will lead to the changing of constitutions and the modification of laws and methods of administration, until the people of every American State shall enjoy the blessings that will flow from a just and simple system of state and local taxation.

To accomplish this result, it is fundamentally necessary that every person participating in the deliberations of this Conference shall say what he believes to be true and give a good reason for believing it, and that he shall not rob others of their opportunity, by taking more than his share of time for the saying of it.

I have the pleasure of introducing Mr. George E. Pomeroy, President of the Ohio State Board of Commerce, who will act as temporary Chairman of this Conference. — Mr. Pomeroy.

Mr. Pomeroy in accepting the temporary chairmanship spoke as follows:

MR. POMEROY:

Mr. President, Your Excellencies, Ladies and Gentlemen:

We are all impressed with the importance of this Conference. It has gathered strength from the time of its inception. It has

widened in interest and scope until we feel assured that the intention with which it was called is to be more than fulfilled.

Most of us have thought of taxation as a burden, but taxes properly levied should not become a burden. Good citizens will bear taxes, if properly and proportionately levied, as they bear any other fixed charge. We should have as much gratification in expending money levied for taxation as we would have in our own private interests, in beautifying our homes, our streets, our parks, our cities. The President of this Tax Association, appreciating the great value of the aid given to this Conference by Governor Harris, has addressed to him the following letter:

"COLUMBUS, OHIO, November 8, 1907.

"GOVERNOR ANDREW L. HARRIS,

"COLUMBUS, OHIO.

"My dear Sir:

"I take advantage of the opportunity offered in sending you the inclosed copy of the program of the National Conference on State and Local Taxation, to express to you my sincere and profound appreciation of the aid you have rendered by your coöperation in organizing this Conference. I believe that the results of the Conference will be a great and lasting benefit to the people of Ohio and of every State in the Union, and that the part you have taken and are to take in it will be to you a source of great satisfaction throughout all your remaining years.

"Yours respectfully,

"ALLEN RIPLEY FOOTE."

It has been a source of great gratification that our Governor, with his hard-headed common sense and practical mind, has seen fit to take up the study of this great question of taxation, and has coöperated with the management of this Association so forcefully and so successfully in bringing about this Conference. The Governor of Ohio needs no introduction from me. We all know him as the first figure in public life in this State. I am pleased to present to you Governor Andrew L. Harris.

Governor Harris was greeted with applause, and delivered the address of welcome as follows:

GOVERNOR HARRIS:·

Mr. President and Commissioners of the National Conference on State and Local Taxation:

I esteem it a great honor to appear before you to-day and bid you welcome to the State of Ohio.

It has been my privilege during the past year or more to welcome various organizations to our commonwealth. Many of them were national conventions and assembled here to confer on questions of interest to their own pursuits and purposes individually and collectively. This Conference is not in the interest of its members. It has no selfish purpose. It is in the interest of the people. You have assembled on your own time and at your own expense to confer on one of the most important business questions now before the American people. You cannot be interested more than your neighbors.

You are here to try to solve the great problem and suggest ways and means by which the burden of taxation will fall equitably upon all. The demands for revenue are increasing more rapidly than the taxable property that is found and placed upon the duplicate. The rate is increasing year by year and that causes more and more intangible property to go into hiding, thereby escaping the burden of taxation until one of high authority has said there is an urgent need, for the sake of public morality as well as of public economy, that all intelligent citizens should inquire how our taxation may be reformed in the interest of equity, truth and righteousness.

The situation seemed to demand a national conference of tax experts, and the President of the National Tax Association accordingly made the call and fixed this date for coöperative consideration on the part of the different States. To aid this Association in the efforts set forth in the call, I requested the Governor of each State to appoint three commissioners to attend this meeting as the representatives of their respective States. The President of the Association has invited all Auditors or Comptrollers of State, all members of State Tax Commissions, all members of Boards of Equalization, the Presidents and Professors of Economics of all of our universities and a large number of persons prominent in public and business affairs through-

out the country to attend and participate in the deliberations of this Conference.

These invitations have been so generally and favorably responded to that we have now, by your presence, in numbers and in ability the largest and best Conference of the kind that has ever assembled in the United States. The large number of papers on the various subdivisions of the subject of taxation, which have been carefully prepared and will be presented to you, is additional evidence of the interest that is manifested in this subject. I have no doubt you will be able to meet the most sanguine expectations of the people and attain the purposes for which this Conference was called. I trust before you adjourn that you will be able to furnish to the legislatures of the several States a concrete statement of the principles that should be applied in state and local legislation, and that the same will be used as a guide for the action of the different States when they are considering propositions to improve their tax laws and develop, as far as possible, a higher degree of uniformity in such laws. I also trust that there may be such uniformity in tax legislation as will eliminate the evil of temporary changes in residence and in the location of business undertakings induced by existing differences in state tax laws.

Appreciating your attendance here as members of this Conference, and realizing the magnitude and importance of the work before you and the large number of able addresses from specialists that you will have presented for your consideration, I will not detain you further than to again extend to you a hearty and sincere welcome and wish you a harmonious and profitable session. I assure you we will ever hold in kind remembrance your stay among us and wish for you and yours health and happiness at your respective homes.

Mr. Pomeroy requested Mrs. Mary C. Snyder, Secretary of the National Tax Association, to act as secretary, and Miss Antoinette Jackson to act as the official stenographer.

MR. POMEROY:

The importance of this meeting is further exemplified by the willingness of the Governor of Massachusetts to accept the posi-

tion of permanent Chairman and to preside over the deliberations of the Conference — even signifying his acceptance during the heat of a campaign in his State, the result of which was to return him to the executive chair by the wonderful majority or plurality of one hundred and five thousand votes. (*Applause.*)

I am honored in being able to introduce to you Governor Curtis Guild, Jr., of Massachusetts, as your permanent Chairman. (*Applause.*)

In response, Governor Guild said:

GOVERNOR GUILD:

Mr. Chairman, Mr. President, Your Excellency and Gentlemen of the Conference:

I thank you for your very kind reception. I deem it a great privilege to stand here to-day and to speak, not only for the other States of the Union, but for the guests and members from beyond the borders of the United States, for surely never more than at this time do free American citizens of the United States welcome with enthusiasm free American citizens of the Dominion of Canada. (*Applause.*)

In the name of the assembled delegates, Governor Harris, I thank you most heartily for the ever generous hospitality of the great State of Ohio—Ohio, the mother of presidents. Perhaps no other State than Massachusetts, mother of States, has a greater right to share, possibly to lead, in this address of thanks for your kind hospitality. It was, you will remember, a Massachusetts soldier, General Rufus Putnam — he who drew up the plans and laid out the fortifications at Dorchester Heights, whose cannon drove the last foreign invading force from New England soil, who won the first, not Massachusetts victory, but the first victory of the united American people—it was this same Rufus Putnam, who, in 1788, as the head of the Ohio Company, led the East to the Northwest Territory. It was this same Ohio Company which, in the splendid Ordinance of 1787, anticipated by nearly one hundred years the emancipation proclamation of Abraham Lincoln, declaring that north of the Ohio River slavery should be forever prohibited.

If the original intention of the founders of the Ohio Company had been carried out, the first settlement in Ohio would not

have been called Marietta, but Adelpia — brotherhood — in token of the brotherhood north and south, east and west, that exists among all the States. In that spirit we come here to-day, not as jealous representatives of merely federated and rival commonwealths, but as citizens of one great common country and nation, seeking the common advantage of all countries, the common interests of all States, though coming as we do from separate commonwealths, whose separate flags fly beneath only one — the Stars and Stripes of the United States of America. (*Applause.*)

The spirit of the new national life cannot be checked. We recognize it not merely by the steady advance on lines of national legislation, but by conventions such as this, seeking at least uniformity of theory, uniformity of law in lines where the national Constitution may bar national action. Each State has its own natural advantages, and we are slowly but surely acquiring, not a New England conscience, nor a Southern conscience, nor a Northwestern conscience, nor a Pacific Coast conscience, but an American conscience that in time will prohibit bad or weak law in any one State from causing injury or injustice in any other State.

If the profanation of the American home by loose divorce laws is condemned in most States, it should not be possible for any one State to spread such poison through the others.

If it is a menace to citizenship that the children of the nation should be starved in body and mind by the substitution of the padrone or the mill superintendent for the schoolmistress, then there should be no one State in the Union able to attract investment from the others by the sacrifice of the labor and lives of little children on the altar of dividends.

If it is wrong that the American people should be forced to pay in higher freight rates, in higher passenger rates, in higher retail prices for commodities in universal use, a perpetual income on capital never invested, rewards on risks never taken, then it is unjust that the weak corporation laws of any one commonwealth should be permitted to set at naught, as they do to-day, justice and equity to the people of the entire United States.

It may come to a more general adoption of national legisla-

tion, but before that desperate means is tried, it is worth while to attempt, at least, uniform state legislation.

We are passing through a peaceful but irresistible revolution. The old order changes. The old barriers are burned away. Public opinion is restless, almost hysterical.

"Give me neither poverty nor riches," cried the proverb maker of Israel. The avoidance of all extremes is the cardinal duty of the man in public life to-day. On one side is the Scylla of corporation corruption. On the other is the Charybdis of destructive demagogism. The future belongs neither to the corruptionist nor to the demagogue, but to those apostles of fair play who demand justice from labor to capital, justice from capital to labor, and who recognize that the whole question is not stated if we do not add justice from both capital and labor to the public, which pays the dividends of the first and the wages of the second. In that spirit, in the new spirit of Nationalism, we are met to discuss the broad question of taxation.

With the possible exception of municipal rule, taxation is the phase of popular government in which the United States so far has made its most conspicuous failure. We have a certain fixed system of internal revenue and of customs dues as a source of national income, but beyond that is chaos. The various States differ among themselves as to which kind of impost should be devoted to state and which to local revenue. There is absolutely no uniformity in taxation, and industries are transferred from one commonwealth to another by the exemption from taxation in certain States of classes and corporations that cannot be exempted under local laws in other States.

The time is ripe for a clear understanding among all the commonwealths as to:

1. What methods of taxation are and what are not desirable?
2. Of desirable methods of taxation, which are the fairest and most practical?
3. Which taxes should be reserved for national and which for state or for local revenue?

The President of the United States in his message to the last Congress suggesting a national inheritance tax and a national graduated income tax has touched upon a great evil. It is true that a state or city tax that presses hard upon the inheri-

tors or possessors of great fortunes may, in our present utter lack of uniformity in taxation, be readily avoided by a tax dodger who chooses to take out a legal residence in another city or in another State. It is just, also, that the possessors of hundreds of thousands as income should be taxed not merely actually, but relatively, more than those possessed of a more modest revenue.

To secure at once the reform of the abuse suggested and a greater measure of justice, is it, however, necessary that there should be either double taxation or that state and city treasuries should be deprived of well-established sources of local revenue by new national taxation of incomes and inheritances for the benefit of a national Treasury now burdened with a surplus?

The Supreme Court of the United States has already declared a national income tax unconstitutional. The income tax, theoretically, is the most just of all taxes. Nobody disputes that a local income tax is constitutional.

Before resorting to the desperate remedy of national laws, possibly involving a violation of the national Constitution, and certainly taking from the States the sources of revenue assigned to them from the beginning, is it not worth while to try for uniformity of state law that nowhere in any one State may the tax dodger find release from the full contribution which he owes to the government which at once protects his enterprise and his fortune? May we not help equity, common sense and the just distribution of the burdens of government by establishing uniform standards of state taxes, uniform standards of local taxes and a national limitation of national taxes?

Taxes theoretically, moreover, are the thermometer by which the people is supposed to judge whether it is expensively or economically governed. Actually they are nothing of the sort.

Take, for example, the poll tax assessed on the sound theory that every citizen should pay something, if only a dollar a year, toward the support of the government. In practice it simply means an extra charge on those already assessed for other taxes. It is purely a class tax, just in theory, unjust in practice. It is not paid in the large cities because the expense of each collection is more than the amount due as poll tax from the wage workers whose modest incomes are exempt from other forms of

taxation. On the other hand it is paid in the country towns by the farmer, whose net income may be no larger than a machinist's or a boss weaver's, but who is assessed, not only for a poll tax, but for a tax on his real estate, his farm. The town clerk informs me that in Barre, a typical farming town of Massachusetts, ninety per cent of the voters pay at least a poll tax, while in Boston, with one hundred thousand voters, never fully one half, usually less than a third, contribute one cent directly to the support of the government. In other words, the policy and government of a great city are controlled by an overwhelming majority of voters who pay no taxes whatever, or at least, but a small head tax that is the same, regardless of the expense of government. I believe this fact is the root of evil local government.

The demagogue in the great cities can afford to ignore the discussion of extravagance that never hits directly at the masses. Padded pay rolls and corrupt contracts do not seem to hurt the average city voter. They may mean a job without work for this voter's cousin, or a contract with thousands in it for distribution to that voter's employer. The people pay in the end, of course, for indirectly somebody has to pay for extravagant furniture and paint bills, for armies of loafers supported in joyous idleness at the public expense. Usually it comes out of real estate. The tenement house owner pays the added tax for his house, and raises his rents. The provision dealer pays it for his shop, and raises the retail price of steak. The non-taxpaying voter pays his increased rent with a curse, not at his own foolish vote for a corrupt government, but at the capitalist landlord who, he has been told, is grinding the faces of the poor. His wife returns from market with similar criticisms on the duty on beef, which is, of course, absolutely inoperative and utterly without effect on the prices. Neither appreciates that the extra dollar for rent, or the high price of steak, goes, in the shape of taxes, to support armies of political barnacles for doing no service beyond sticking to "the organization."

The absence of any broad, rational, logical, uniform system of taxation for city, State and nation is not only unjust theoretically, but absolutely destructive to intelligent voting on the merits of government, the very foundation stone of any republic.

Let us hope from this Conference may issue some general classification of sources of revenue and their special applicability to local, state or national revenue, some recommendation as to uniformity of auditing and bookkeeping in all the States, some recommendation as to the general abolition of inequitable taxation and the uniform adoption of more equitable laws by all the States, in which the burden of government shall bear more easily upon the weak, more heavily upon the strong, but at least so universally that weak and strong may alike appreciate when government is bad and when it is good, that our government of public opinion may be government by a more acutely intelligent public opinion.

This, I say, is an age of social evolution, almost an age of revolution. The old barriers are being burned away, and we are seeking, not only on the line of taxation, but in other lines as well, a better chance and better equalization of public burdens. Never has there been a time when our country has stood where it does to-day. We stand, although we may not appreciate it, at a time of great crisis in the development of our country. We have had two such crises before; and when the history of the first hundred and fifty years of our country shall be written, it will be appreciated that not two, but three, men have been called to guide our country through perilous times—two crises in war, one crisis in peace. The Constitution guarantees to all people life, liberty and the pursuit of happiness. George Washington gave this nation life; Abraham Lincoln gave this nation liberty; and Theodore Roosevelt has given this nation an equal chance in the pursuit of happiness. (*Applause.*)

The Convention will come to order. The first business before us is the nomination of three Vice Chairmen.

MR. DUBUQUE (Massachusetts): Mr. Chairman, I move that Governor Dawson of West Virginia be selected as the first Vice Chairman of this meeting.

The motion was seconded and unanimously adopted.

MR. ADAMS (Wisconsin): Mr. Chairman, I take great pleasure in nominating for the second Vice Chairman, A. C. Rutherford, Premier of Alberta, Canada.

The motion was seconded and unanimously adopted.

MR. FOOTE (Ohio): In behalf of Ohio, I wish to nominate as Vice Chairman, William O. Thompson, President of the Ohio State University.

The nomination was seconded and on vote unanimously carried.

GOVERNOR GUILD: I am sure the gentlemen of the Conference would not forgive me if I did not at this time ask for a word from those whom you have chosen as Vice Chairmen, and I therefore take great pleasure in presenting to you one who as the chief executive of a neighboring State is certainly well known to the people of Ohio, and one whose qualities, wherever he has been known, have endeared him to the people of the United States — Governor Dawson of West Virginia.

Governor Dawson was greeted with applause, and responded to his selection as Vice Chairman as follows:

GOVERNOR DAWSON:

Mr. Chairman, Mr. President, Governor Harris, Delegates and Ladies and Gentlemen:

This is very unexpected to me. I have been congratulating myself that my name does not appear on this program, for I did not notify President Foote that I would be here until yesterday about noon; but I thank you for the honor, which I know is intended not for me personally, but for the great State of West Virginia. I am a Virginian, and I shall not take your time now to argue out with the Governor of Massachusetts the proposition that Ohio is the mother of presidents. (*Laughter.*) We will settle that privately. But not even Ohio will dispute that Virginia is her mother and gave her this great territory.

I am delighted, Governor Harris, to be in the great State of Ohio; I am sure that I am welcome, because, as I am already an officeholder, I cannot enter into competition with your people upon that question. (*Laughter.*) I am glad to be in the great State of Ohio, because it is a great State, a progressive State, and if Governor Guild will pardon me, I know of no place where it is more fitting to hold a Conference of Tax Reformers than in the State of Ohio. (*Applause.*) I hope my remarks

may not be misconstrued; I do not mean that Ohio needs it more than any other State, but because of your progress here and because of the general high average of the intelligence of your people, it is fitting that it should be held here. We have had a little contest in the State of West Virginia in the last four years about this same question of taxation, and we are still in the fight. We think we have passed the middle of it and that the worst is behind us, and we congratulate ourselves that we have made some progress; but we shall be better able to judge of that, I fancy, after we have heard the conclusions of this assembly.

I need hardly say that the question of taxation is the greatest of all public economic questions; it is fundamental, and it is something that has taxed the minds of men from the earliest dawn of history. I know of no better index to the character of a people as regards their advancement in culture and civilization than the state of their system of taxation.

Now, gentlemen, I am admonished by what I have seen and by what has been said to me, that I must be brief; I merely beg to take enough more of your time to say that I greatly appreciate the honor you have conferred upon me, and thank you most sincerely for it. (*Applause.*)

GOVERNOR GUILD: Massachusetts is ever ready to praise Virginia as well as Ohio as the mother of presidents, and we shall not dispute in regard to the claims of Virginia and Massachusetts as the parent of Ohio; we are glad to know, as just proved by the Governor's remarks, that Ohio may boast of a father as well as a mother. — I shall take great pleasure in now presenting to you one who has very kindly consented to speak in behalf of the Premier of Alberta, Canada, who is unfortunately detained and cannot be here at this time; but we are highly favored in having with us another Canadian statesman, and I am pleased to present to you the treasurer of the great province of Ontario, Canada, Honorable A. J. Matheson. — Mr. Matheson.

Mr. Matheson, in acknowledgment of the selection of Mr. Rutherford as Vice Chairman, spoke as follows:

MR. MATHESON:

Mr. Chairman, Your Excellencies, Ladies and Gentlemen:

In behalf of the Honorable Mr. Rutherford, Premier of the province of Alberta, and in behalf of the Canadian people, I beg to thank you for the great courtesy which the State of Ohio, her Governor and the members of this Conference have extended to us in inviting us to be present at this meeting. I hope that Mr. Rutherford will be here to answer for himself to-morrow. You know, I have no doubt, that the province of Alberta is on the border of our northwest, extending from the boundary line for four hundred miles and from the eastern range of the Rocky Mountains some three or four hundred miles eastward — one of our new provinces only formed last year; and Mr. Rutherford will be especially anxious to listen to the debates of this great Conference. Our constitution, as you are aware, is somewhat different from yours, and he is not only prime minister, but he is a member and leader of the House of Assembly of Alberta, in the same way that in our province we, who are ministers in charge of a department, are members of our legislature. We are responsible to the people. No member of that legislature could propose taxation of any kind without the message of the Governor, which is given on the advice of his ministers; and that is where I come in, because on matters of finance the treasurer of the province is supposed to advise as to what measures of taxation should be gone into — should be enforced. We have a government that must have the majority of the legislature. If a motion is made by the opposition of want of confidence in the government, they have to resign, and the members of the opposition are called upon to form a new government. I do not wish to trespass upon your time, gentlemen, but again I wish to thank you for the opportunity of being present to hear these discussions. To a certain extent, our legislation affects you and your legislation affects us. You might not think so, but take your inheritance tax: take the case of a citizen of New York who owns stock in a company in the province of Ontario; is it right that his estate should, as an inheritance tax, pay taxes both in New York and Ontario? Or take the reverse case; is it right that the estate of a citizen of Ontario, administered in Toronto, owning stocks in New York, should pay

the inheritance tax on that stock in New York and also in the province of Ontario? Those are questions that are coming up and will come up in this Conference as between States. We have a satisfactory provision in our inheritance law which provides that in the case of stocks in New York or any other State held by a person's estate administered in Ontario, we allow off our taxes the amount paid in New York, provided that New York, in a similar case, allows the Ontario tax off in case of the New York citizen owning Ontario stock; that, however, is a matter for your discussion, but it shows how great an interest we have in taxation and in the discussions that are to take place here.

Again I thank you, Mr. President, Governor Harris of Ohio, and you, gentlemen, for the great courtesy that you have extended in your invitation to us, and for the honor you have done the Dominion of Canada in appointing one of our representatives one of your Vice Presidents. (*Applause.*)

GOVERNOR GUILD: We have received a message that President W. O. Thompson of the Ohio State University will be unable to reach here this morning. We will therefore proceed to the other regular business of the session.

MR. POMEROY (Ohio): Mr. Chairman, before we proceed with the regular business of the session, I desire to present to you in behalf of and in the name of the Tax Association, this badge, as Permanent Chairman of this Conference on State and Local Taxation.

GOVERNOR GUILD: I thank you very much, sir, and the Tax Association for this unexpected and very beautiful souvenir; I shall keep it always with the greatest gratitude. I shall appreciate it the more because it was given to me in Ohio, the home of a very dear friend. As delegate at large from Massachusetts, it was my privilege to stand by him in the campaign of 1896, all through the summer and the fall, along the line of the single gold basis; and I am delighted in this beautiful gold badge, this gift, to recognize not only the stand taken by Ohio for honest money, but the revered memory of William McKinley. (*Applause.*)

The next business before the Conference is the appointment of a Committee on Resolutions.

MR. PURDY (New York): I move that the Chair appoint a Committee on Resolutions and Conclusions composed of one member from each State and each Province represented in the Conference.

The motion was seconded and carried by unanimous vote.

CHAIRMAN GUILD: The Chair will announce the Committee later. The next business before you is the appointment of a Committee on Program and Rules.

MR. PLEYDELL (New York): I move that the Chair appoint a Committee of five on Program and Rules.

The motion was seconded and carried by unanimous vote.

MR. POMEROY (Ohio): I move you that all resolutions presented shall be referred without debate to the Committee on Resolutions and Conclusions.

The motion was seconded and carried by unanimous vote.

[At a subsequent meeting.]

GOVERNOR GUILD: Gentlemen, before proceeding to the reading of papers I wish to announce the Committees.

COMMITTEE ON PROGRAM AND RULES

A. C. PLEYDELL, Chairman, New York; Secretary New York Tax Reform Association.

FRANK G. PIERCE, Marshalltown, Iowa; Secretary League Iowa Municipalities.

E. A. ARMSTRONG, Camden, New Jersey; Member State Board of Equalization and Taxation.

T. D. ROCKWELL, Spokane, Washington; Chairman State Tax Commission.

N. S. GILSON, Fond du Lac, Wisconsin; Chairman State Tax Commission.

COMMITTEE ON RESOLUTIONS

CHAIRMAN, Lawson Purdy, New York

United States:

Arkansas	George B. Curtis	Harrison
California	Harry A. Millis	San Francisco
Colorado	J. B. Phillips	Boulder

Connecticut	William H. Corbin	Hartford
Dist. of Columbia	L. G. Powers	Washington
Georgia	E. C. Kontz	Atlanta
Illinois	Frank P. Crandon	Chicago
Indiana	W. H. Paddock	Indianapolis
Iowa	Isaac A. Loos	Iowa City
Kentucky	William A. Robinson	Louisville
Maine	George Pottle	Lewiston
Massachusetts	Guy W. Cox	Boston
Minnesota	F. L. McVey	Minneapolis
Missouri	F. N. Judson	St. Louis
Montana	J. H. Underwood	Missoula
Nebraska	George Bennett	Lincoln
New Hampshire	William B. Fellows	Concord
New Jersey	C. C. Black	Jersey City
New York	Lawson Purdy	New York City
North Carolina	B. F. Dixon	Raleigh
North Dakota	J. E. Boyle	Grand Forks
Ohio	W. D. Guilbert	Columbus
Pennsylvania	J. W. Langham	Harrisburg
South Dakota	Carl W. Thompson	Vermilion
Tennessee	J. D. Hoskins	Knoxville
Texas	L. M. Keasbey	Austin
Utah	J. J. Thomas	Salt Lake City
Vermont	E. L. Hitchcock	Pittsfield
Washington	J. E. Frost	Olympia
West Virginia	T. C. Townsend	Charleston
Wisconsin	T. S. Adams	Madison
Wyoming	William R. Schnitger	Cheyenne
Canada:		
Alberta	A. C. Rutherford	Edmonton
Ontario	Prof. Adam Shortt	Kingston
Quebec	E. Stewart Dunlop	Montreal

[At a subsequent meeting.]

GOVERNOR GUILD: We will now hear the report of the Committee on Program and Rules, Mr. Pleydell, Chairman. Is that Committee ready to report?

MR. PLEYDELL:

The Committee on Program and Rules asks leave to report the following recommendations:

1. That when this Conference resolves itself into a business session to receive the report of the Committee on Resolutions and take action, the ordinary rules of parliamentary procedure shall govern.

2. That the voting shall be confined to the delegates appointed by governors and universities as outlined in the printed program, and shall be by ayes and nays unless otherwise demanded.

By unanimous vote the report of the Committee on Program and Rules was received and adopted.

A COUNCIL OF STATES

BY DR. CHARLES A. L. REED, UNIVERSITY OF CINCINNATI,
CINCINNATI, OHIO

- I. A Council of States.
- II. Progressive Laws for Progressive People.
- III. Like Laws for Like Conditions.
- IV. Unlike Laws for Unlike Conditions.
- V. Unlike Laws for Like Conditions.
- VI. Our Great Inland Trade.
- VII. State Laws in Restraint of Trade.
- VIII. The Voice of Protest.
- IX. Federal Aggression — President Roosevelt Justified.
- X. The Loss to the States.
- XI. A Coördinating Mechanism necessary in Coördinate Action.
- XII. The Congress incompetent to Act.
- XIII. Remedial Tendencies.
- XIV. An Important Precedent.
- XV. States may initiate Amendments to the National Constitution.
- XVI. Influence of a Council of States on Constitutional Amendments.
- XVII. The Council of States — How Established.
- XVIII. Composition and Duties.
- XIX. A Warning to the States.

THE object of my remarks is to propose the assembling of a Council of States. The first purpose of such a council would be to formulate standard bills, not only on taxation, but on all other subjects, of pressing importance, and submit them for enactment in uniform terms by the state legislatures. Its next purpose would be to act in an advisory capacity in respect of any and all other subjects, concerning which it is desirable that the States either adopt uniform constitutional provisions, or enact uniform laws, or arrange uniform rules, regulations, procedures and practices for the enforcement of existing laws.

It of course goes without the saying that the functions of such a body would be restricted to the consideration of subjects which the nation in the exercise of its sovereignty has placed, for the time being, within the purview of the States, as contradistinguished from those other subjects which it has similarly placed within the jurisdiction of the federal government. It likewise goes without the saying that such a body, to fulfill the objects for which it would be called into existence, must be made up of men of highest ability, selected geographically and in numbers on a representative basis. And it must meet, as a legislature or the Congress meets, in a session or sessions sufficiently long and deliberate to be productive of sound results. Of these not the least would probably be the purely incidental determination, from the view point of the States, of the powers, if any, that ought to be shifted by constitutional means from the States to the federal government, or from the federal government to the States.

PROGRESSIVE LAWS FOR PROGRESSIVE PEOPLE

In support of this proposition, I ask you to indulge me in what I trust shall prove to be a calm survey of the situation, and a brief but, I hope, accurate estimation of at least a few of the many factors involved in the problem. And we may as well begin with a principle as with an incident. Thus, it is entirely outside the controversial to say that the very fundamental object of government is to subserve the social and commercial welfare of the governed. It is likewise true that the strength and durability of any government or of any feature of any government is in exact proportion to its ability to measure up to this standard. Furthermore, it is the duty of the sovereign to change a government in form or feature by taking from or adding to, whenever such government fails to facilitate that progress which is essential to the highest welfare, social and commercial, of the governed.

LIKE LAWS FOR LIKE CONDITIONS

Applying these principles to our own country, let us consider them in relation to some rather important facts. And the first fact that I wish to emphasize is the fact of the nation

itself. I mention it only because its importance and its relations are sometimes not understood — strange as it may seem. There are but few people who realize that the nation is neither the federal government, nor the state governments, nor all of them combined.

The nation consists of all of the people, native and naturalized, living within the encompassing lines of our country. With the nation rests all power — power even to give, change and take away constitutions. The nation is supreme. It is the sovereign. Its sovereignty was, is and will remain one, undivided and indivisible, without line of cleavage or prospect of segregation. The next fact is that it — this nation — then fewer in people and smaller in area, in the exercise of its sovereignty, even then, as full, as ample and as complete as it is to-day, established a unique form of government. It recognized that it had some eighteen or twenty interests that were identical in every part of the country, and these interests it specified in a constitution which it confided to a general government. It recognized, on the other hand, that it had other interests that were variously peculiar to the different groups, some thirteen in number, into which it was at that time accidentally divided. It accordingly left these various interests to be administered by its thirteen component groups, living, as it so happened, in thirteen different States. When, however, the nation made this division of power, it expressly reserved, as the sovereign could not help reserving, the right to shift these powers of government whenever and in whatever particulars it might see fit for the purpose of subserving its — the nation's — the sovereign's — own interests. As a matter of fact it has seen fit to modify the original arrangement some fifteen times. In every instance, however, in which the federal government has been empowered, originally or anew, to deal with general interests, the nation has definitely recognized the principle that like conditions require like laws.

UNLIKE LAWS FOR UNLIKE CONDITIONS

Now, why did the nation give certain powers to the general government and certain other powers to the state governments? Or, to avoid the theoretically political aspects of the inquiry,

what, in 1790, were the conditions in the different States that required separate governments, and more or less different laws for each of them? Their differences, social, religious, political and economic, were in fact many and pronounced. They began at the beginning of the colonies, and continued through the decades, twenty or so, simply because the detachment and isolation of the communities, now grown into States, favored the perpetuation of original types, ideals and impulses. The social and religious differences were thus simply the differences between Cotton Mather, Roger Sherman, Peter Stuyvesant, William Penn, Lord Baltimore, John Smith, and Sir Walter Raleigh. It was a long time before these isolated communities became either neighbors or neighborly. Until long after the Revolution, it required more time, labor and expense to go from any one of the States to any other State farthest removed from it than it now takes to go from Maine to Oregon. Education, fostered in certain States, was purposely repressed in others. Domestic commerce was indeed a "home trade" consisting chiefly in the exchange of commodities within the confines of the respective States where local conditions called for equally local regulations. The labor conditions of Virginia, contrasted, for instance, with those of Massachusetts, required different laws. We see, therefore, that the nation, in giving to each State the right to make its own laws, for its own purposes, recognized the principle that unlike conditions require unlike laws.

UNLIKE LAWS FOR LIKE CONDITIONS

I have just spoken in a most general way of conditions as they existed when the nation established its dual government. What has happened since 1789? And to what extent do or do not the laws of the States conform to these conditions? It is true that Whitney had invented his cotton gin, and Cartwright his power loom, the first five and the latter four years before the Constitution was adopted, but neither invention had yet had time to exert an appreciable, much less a prophetic influence on the industries of the country. It is likewise true that John Fitch, two years before that date, had built a steamboat, and subjected it to successful trial on the Delaware; but the experiment was not taken seriously until, just twenty years later,

Fulton reduced the practical application of steam for purposes of navigation to a demonstration. It is furthermore true that a half century or so had elapsed since Franklin drew the lightning from the clouds, yet it required an additional forty-six years before Morse invented the telegraph, and nearly ninety years before Graham Bell invented the telephone. The constitutional convention had adjourned thirty-six years, and the majority of its members were dead, when Stephenson's locomotive made its first trip from Stockton to Darlington, in England. It was half a century and more before Elias Howe devised the sewing machine, although this invention had been preceded more than forty years by the Hoe perfecting printing press. These were revolutionizing innovations, and were, as they and the improvements that they have bred are to-day, the mainsprings of our great manufacturing and commercial interests.

OUR GREAT INLAND TRADE

There was, of course, some trade between the colonies, as between the original States under the articles of confederation. But our great inland trade, that great volume of trade that has come to be known as "interstate commerce," began with and has steadily followed the completion of the Erie Canal, the Cumberland Canal, the Ohio and Lake Erie Canal and the great National Road — our own Appian Way — almost a hundred years ago, but at least two decades after our governmental forms had been cast. But in 1829 came the steam railway in America. Then came transition. Distances shriveled, time shrunk, commerce leaped, culture disseminated, wealth diffused, industry abounded and neighborhoods previously foreign to each other became linked together in bonds of intimacy. This has gone on until to-day, with a territory more than quadrupled in area, with States multiplied to forty-six in number, with a population twentyfold greater than at the beginning of the government, we find, instead of general diversity, a practical uniformity of conditions. Now, while these changes have been in process of an evolution so rapid at times as to suggest revolution, each State, acting for itself, without reference to any other State, or to all other States, and especially, without reference to the

changing order of things, has gone on making laws relating to every power originally left within its purview by the nation itself. As a consequence, so far as the States are concerned, we are treated to the anomalous spectacle of an increasing unlikeness of laws being enacted for the government of an increasing likeness of conditions.

STATE LAWS IN RESTRAINT OF TRADE

The inevitable has followed. We are to-day confronted by results which, to use the mildest of terms, are embarrassing to the commercial and social interests of the people; results which, if permitted to develop in the direction of natural and logical progression, must become disastrous in their ultimate phases. Already the voice of protest is heard from every section of the country. Corporations, the most useful as they are probably the most dangerous forms of modern commercial activity, incorporated in one State, are, by virtue and in consequence of that fact, subjected to onerous and arbitrary regulations in other States. Railroads, the very makers as they may become the very sappers of our prosperity, are forced to conform to as many classifications of freight and as many other sets of "regulations" as there are States traversed by their lines. Manufacturers of food products are compelled to conform to a different branding and labeling law in practically every State reached by their trade. Distillers of pure liquors are subjected to similar annoyance by the diversity of state license laws. There is no uniformity of state laws relating to bills of lading, none concerning partnership, none governing certificates of stock, concerning all of which there is confusion, with more or less resulting hardships. Insurance laws are in an almost hopeless confusion. State tax laws seem to have been formulated on a policy of punishments and reprisals. Unequal and unjust state laws of sanitation and quarantine have at times led not only to animosities, but to armed demonstrations between neighboring commonwealths. Labor laws of certain States, enslaving in their effect upon children, seem to have been enacted as invitations to predatory industries from other States. A person having qualified in one State as a member of any of the professions or occupations now subject to licensure must, on removing to another State, procure another

license based on different, and for that matter generally arbitrary and unfair requirements. Our diverse laws of marriage and divorce are the opprobria of American legislation. Instances could thus be added to instances, until the list would be too long for recital. But I have said enough to show that the present condition of our state laws is hurtful to the people; for harm done directly to classes, to economic and social groups, is secondarily or later disseminated and visited upon all of the people. It has, indeed, seemed to me at times that no corporation, no combination of corporations, no trust or combination of trusts, is so effectually acting "in restraint of trade" as is this unlikeness, this diversity, in the laws of the different States. But over and above this, the moral influence of the situation, and especially its underlying tendency, is deplorable. I say this for the reason that it involves very much more than mere dollars and cents. It involves, indeed, nothing more or less than the impairment, if not in instances the destruction, of that spirit of neighborliness that we have so long and so fondly thought of and spoken of as "the comity of States."

THE VOICE OF PROTEST

I have said that we hear the voice of protest from various parts of the country. It began eighteen years ago, when New York, the great financial center of the country, found itself especially embarrassed by the then diversity of state laws relating to negotiable instruments, and issued a call for a conference of governors on that subject. Since that time there have been various similar conferences. I recall one in particular, between the governors of the Southern States relative to state sanitation and the exercise of the quarantine power. The recent Trust Conference and the present Tax Conference are but two examples of the general protest. The attorneys-general of the whole country have organized for concert of action, so far as the almost chaotic differences in the laws they are called upon to enforce will permit of action in the prosecution of certain offenders. They have, at the same time, asked the Congress to modify the right of injunction as now exercised by the federal courts to prevent the execution of state laws. State railroad commissioners of the whole country, in convention assembled, have but

recently protested against the further assumption of authority by the federal government in the matter of rates and classifications of freight, and appointed a committee, so the press reports state, "to consider fully what uniformity in legislation is desired or required, and that it meet with committees of Congress and of the various state legislatures." The great railroads, through their traffic department, are ready to coöperate to the same end.

Associations representing the licensed professions and occupations have asked the Congress for national licensure laws until, realizing that power to pass such a law does not lie with the Congress, they are clamorous, and justly so, for uniform laws and consequent reciprocity in licensure by the States.

Distillers are asking for more uniform license regulation of the liquor trade, and a bill to this end was introduced in the Fifty-ninth Congress. Shippers are protesting against the great disparity in state laws relating to bills of lading, and two bills, practically identical, were introduced, one in the House, the other in the Senate, of the Fifty-ninth Congress, which, if enacted, would have taken this phase of the police power from the States. Associations of canners and manufacturers of food stuffs are asking that the States do something to remove the hardships imposed upon that trade by unequal state laws, many of which, at least many of the provisions of which, are recognized as unnecessary and arbitrary supplements of the National Pure Food and Drug Law.

FEDERAL AGGRESSION — PRESIDENT ROOSEVELT JUSTIFIED

We see associations, religious conferences, and conventions and legislatures, such, for instance, as that of Connecticut, memorializing the Congress for uniform laws of marriage and divorce, and a joint resolution declaring for an amendment to the national Constitution, making it possible for the Congress to do this very thing, was introduced in the Senate — another instance of contemplated shifting of existing powers from the States to the general government. A bill introduced in the same Congress to provide for the national incorporation of corporations engaged in interstate commerce was another measure likewise looking toward the abridgment of the existing

powers of the States. A movement for a national insurance law has high governmental support.

The fact is that the Congress and the President are alike subject to enormous pressure to provide a remedy for existing conditions. And it is the duty of both to respond as nearly as possible to this demand. No student of actual conditions can fail to recognize that President Roosevelt is not only justified, but is pursuing a highly patriotic course in his effort to relieve hampered progress by the extension of federal authority over certain important interests heretofore, and nominally at present, falling within the purview of the States. This justification will last until, and only until, the States, by concurrent action, afford uniform laws for the government of uniform conditions over which it is their present duty to exercise authority.

THE LOSS TO THE STATES

If, now, we look at this question of the readjustment of powers between the federal and state governments from the view point of either of them, we are forced to recognize that a shifting of power either way means a corresponding shifting of both revenues and influence. Thus, for example, the revenues now derived from franchise taxes, from licensure and from other exercise of both the taxing and police powers now enjoyed by the States go far toward replenishing their treasuries. These revenues will diminish just in proportion as the exercise of the powers on which they are based diminishes. If new powers are conferred upon the States, — of which, I confess, there now seems but slender possibility, — they would naturally bring with them new and, to that extent, compensating revenues. The influence, the prestige of our States, none too strong to-day in our dual system of government, would be still further lessened just to the extent that old powers surrendered would exceed new powers gained in the scheme of readjustment. These facts being self-evident, and taking into consideration the trend of forces now in operation, it becomes convincingly obvious that the States, unless they take some step that they have not yet taken for the wise and more uniform exercise of certain of their present functions, are destined to forfeit an important part of both the revenues and the influence that they now enjoy.

A COÖRDINATING MECHANISM NECESSARY FOR COÖRDINATE ACTION

The trouble lies obviously with the States. Secretary Root has frankly charged that the States are at fault for the almost aggressive attitude that the federal government has been literally forced to assume with reference to the extension of its powers. It seems to me that if "fault" is to be charged to the States, the word must be used, as I have no doubt that Secretary Root intended, in the sense of failure to meet governmental requirements, and failure, too, in spite of the desire and effort of the States faithfully and efficiently to exercise all of their constitutional prerogatives. The "fault" lies obviously with the nation, which in the beginning failed in this particular, in its purview of its own necessities. As a matter of fact, the States have no means of getting together; no medium for arriving at an understanding; no instrumentality by means of which they may become coöperative in subserving the commercial and social welfare of the governed. In the furtive efforts in this direction that we now behold, we see simply so many necessarily futile attempts at coördinate action in the complete absence of a coöordinating mechanism.

THE CONGRESS INCOMPETENT TO ACT

It is evident from this survey of conditions that the natural impulse of practically everybody interested in the solution of this problem is to turn to the Congress for relief. They naturally feel not only that the Congress is national in its powers, but that it is simply forty-five times less troublesome to get necessary legislation from one legislature which happens to cover the territory of all the States than from forty-five different legislatures with state limitations. Hence the appeals, the pressure on the national government. And neither the legislative or executive branches can ignore the obvious necessities underlying the demand. As a result, and a very natural result, the broadest possible interpretations are being given to the interstate-commerce and post-road clauses of the Constitution as a warrant for the new and unusual exercise of federal powers within the confines of the respective States. But there must be a limit. There is a limit beyond which the

federal government cannot extend its powers without specific authorization by the nation. For, in spite of the great importance attaching to the requirements of commerce, there is no necessity so paramount as a rigid observance of the powers expressed and implied of the Constitution. It is doubtful, in view of this fact, whether or not they who clamor for congressional intervention realize the distinct limitations of congressional powers. They seem to ignore the important fact that the Congress can legislate for the country at large only on special subjects, and that it is entirely foreign to its powers either to legislate or to suggest legislation on the subjects that have been placed by the nation within the purview of the States.

REMEDIAL TENDENCIES

There seems, however, to be a tendency, natural and evolutionary in character, to supply the deficiency that the Congress itself cannot supply. At times these activities seem to be purposely directed movements. Thus, the gubernatorial conferences, the conventions of attorneys-general and of state railroad commissioners, to which I have referred, and the confederations of state examining and licensing boards, whose proceedings are to be found in the prints, are only a few of what in reality must be looked upon as efforts, preliminary and tentative, to evolve some means by which the States, acting as States, may get together and do business in the discharge of their constitutional obligations. The most hopeful, because the best directed and, consequently, the most instructive of these incoördinate movements to a common, if unconscious, end, is that which followed the call of the Governor of New York for a conference in 1890. The call resulted in the organization of the Uniform Laws Commission, which has since met annually in connection with the American Bar Association. Its first fruit was a standard act relating to negotiable instruments, which was promulgated in 1896, and which has since been adopted in uniform terms by thirty-five States and Territories, including the Congress for the District of Columbia. That same year it promulgated a Sales Act; last year it reported a Warehouse Receipt Act, and this year a Marriage and Divorce Act, which, of course, has not yet had time to be acted upon by the legislatures. The

results of the Negotiable Instruments Act are, however, most instructive and encouraging. Adopted by thirty-five leading States, it has to that extent established uniformity of law for the uniform requirements of this particular commercial interest. It is also worthy of note that since the enactment of this law by the States this is the only subject relating, as this certainly does in some degree relate, to interstate commerce that has not been pressed upon the Congress with a demand for the passage of a national law. Why? Simply because the States by this means and in this particular met the commercial requirements of the people. And what is true of negotiable instruments can be made equally true of other interests of equal or greater importance to the people.

AN IMPORTANT PRECEDENT

But a commission such as the one I have mentioned, valuable as it is as the precursor of more important things, cannot fulfill the demands of the times. Meeting as the appenage of a national professional organization, to which it reports, it has neither the individuality, prestige nor contact that enables it adequately to influence the people and through the people their representatives in the legislatures. Assembling but once a year, and then only for a few days, it cannot, in spite of its *ad interim* work in committee, make progress that will meet the requirements of the hour. A record of four small acts promulgated in seventeen long years can hardly be accepted as a demonstration of practical efficiency. It is, however, of incalculable value as the demonstration of a principle and as a precedent for a broader movement. And, furthermore, the very able gentlemen who comprise the commission have been developed by their experience in the direction of special efficiency as members of the proposed council of States — a fact of which the movement and through it the country in general ought to be made the beneficiary.

STATES MAY INITIATE AMENDMENTS TO THE NATIONAL CONSTITUTION

The creation of a coördinating mechanism for the States would, furthermore, enable them to exercise another constitu-

tional prerogative which, for want of such a mechanism, they have never yet been able to exercise in the one hundred and twenty years of their existence. I now allude to the right of the States to take the initiative in proposing amendments to the national Constitution. That instrument itself prescribes two ways by which amendments may be proposed. The Congress may do so by a two thirds majority of both houses; or, if two thirds of the state legislatures by concurrent action request it, the Congress must call a convention to propose amendments. But how can the States, through what existing instrumentality can they, as States, engage in any concurrent action? There have been nineteen amendments to the Constitution so far proposed, all of them through the initiative of Congress. Why? I do not assume that the inability of the States to act, for the reason given, is the sole explanation. The initiative of the Congress and subsequent ratification by the legislatures is obviously the natural and direct way to amend the Constitution under normal circumstances. It is probably the safer way. All publicists have felt, I think justly, that the Constitution should be changed as little as possible, and that a constitutional convention would have a dangerous tendency to go too far in the matter of amendments; that it might, indeed, go to the length recently seriously suggested by one of our college presidents and propose an entirely new Constitution. It has, furthermore, always seemed to me that the method of proposing amendments through the initiative of the state legislatures was only a whip provision to be utilized by the States when, in their opinion, the Congress might need the lash. Fortunately, such a contingency never seems to have arisen, as I trust that it may never arise. But if it were to arise, or if any other reason should arise why the States ought to take the initiative in the amendment of the Constitution, they would be helpless to do it in the absence of some mechanism, such as the proposed council of States.

INFLUENCE OF THE COUNCIL OF STATES ON CONSTITUTIONAL AMENDMENTS

As a matter of fact, the influence of the proposed council in determining which, if any, of the existing powers of the States ought to be shifted to the national government or *vice versa*, of

course by the constitutional means of amendment, would be purely incidental. Thus, if it became apparent, through the deliberations of the Council, that the States could not exercise their existing powers so as to furnish uniform laws for uniform conditions, as applied to particular interests, they, the States, ought to be the first to propose a transference of those powers to the national government. Action by the States to this end need not take the "convention route" as outlined by the Constitution, which would probably be tedious, difficult and dangerous. It could as easily take the form of mere memorials, asking the Congress to proceed by the same methods by which the fifteen existing amendments have been safely proposed and adopted — if, indeed, the Congress, prompted by the proceedings of the Council, did not anticipate such action by the legislatures by taking the initiative itself. In any event, however, the possible influence of the States in the matter of proposing amendments would be enhanced by the creation of some instrumentality that would enable them, as they have never yet been enabled, to act together.

THE COUNCIL OF STATES — HOW ESTABLISHED

It seems to me that the assembling of a Council of States ought to be a matter of no difficulty whatever. The Governor of any State could take the initiative by inviting a conference with the Governors of the other States. This conference could determine four points: first, that a Council of States shall be called, together with the time and place; second, the basis of representation; third, the scope of the proceedings, if not the particular subjects, to be submitted for deliberation; fourth, the approximate expense attaching to the movement. Each Governor could thereupon lay the matter before his respective legislature which, by joint resolution, could concur or nonconcur in the proposition. If the resolution to concur should prevail, it could provide for the election by the legislature or the appointment by the Governor of the prescribed number of delegates, and at the same time provide funds for their honoraria and for the pro rata expense of the meeting. All further details ought to be left to the Council itself.

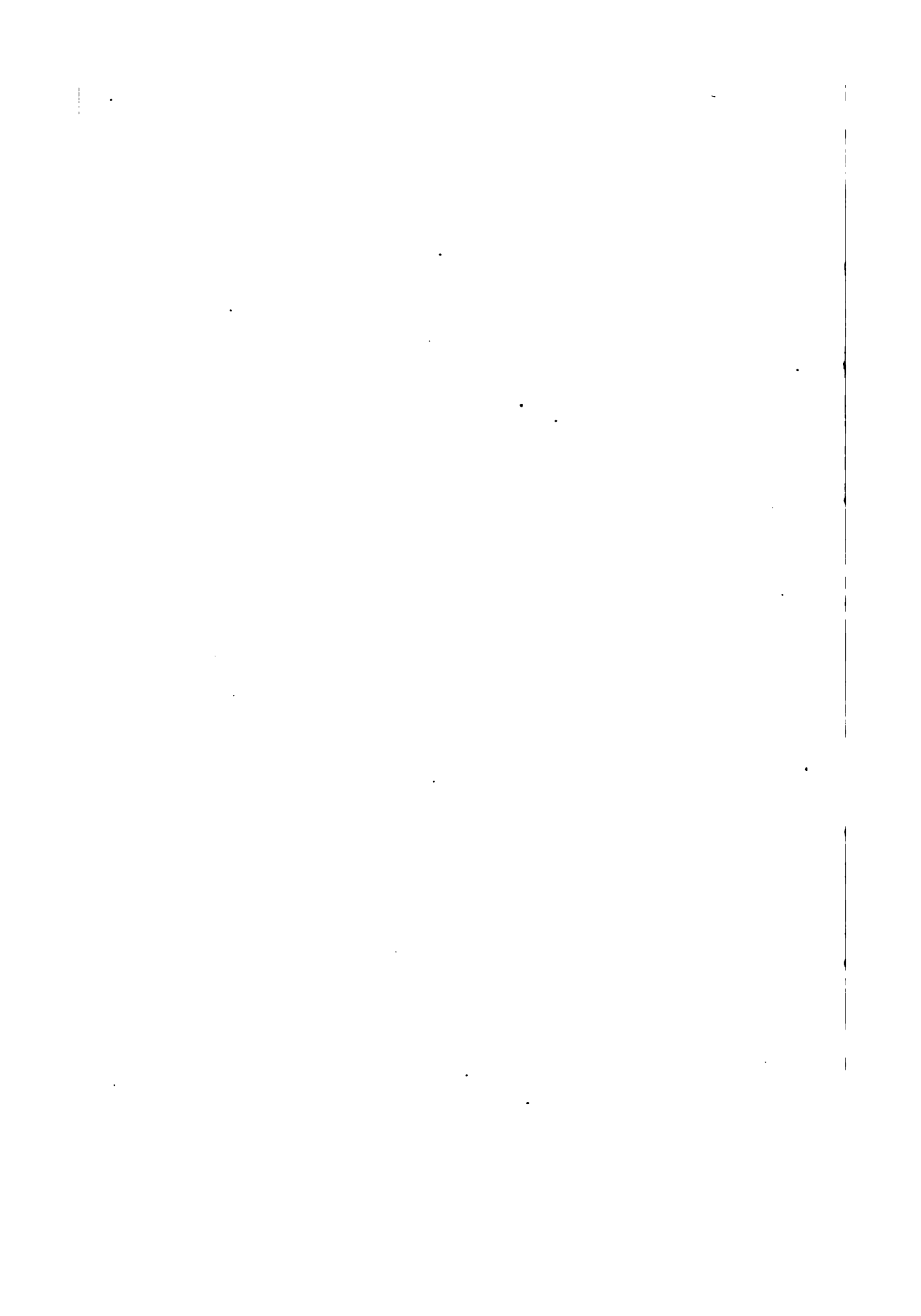
COMPOSITION AND DUTIES

Any capital of any State could serve as the place of meeting during any year when its own legislature is not in session. The Council could meet in 1909, and not sooner, for the reason that all the States could not act on the subject before that time. Only some seventeen legislatures will be in session this year; the remainder will meet the year following. The men chosen ought to be among the ablest in the respective commonwealths. There ought not to be less than two from each State, which would yield a body the size of the national Senate; nor ought there to be more than one from each congressional district, which would yield a body the size of the national House of Representatives. I cannot imagine that a dual body, corresponding to the Congress, ought to be assembled. My personal preference would be for a body of two from each State, together with territorial delegates. Hearings in committee should be held on all subjects. A daily record of proceedings ought to be printed in periodical form. Compensation, whether per diem or a salary, ought to be provided on a basis equivalent to that paid to congressmen, but to be determined in each instance by the States themselves. The session, whether broken by adjournment or not, ought to last until the purposes for which the Council shall have been called have been accomplished. The fruits of the deliberations of the Council should be laid before the legislatures by their respective delegates. The prescription of duties should embrace this feature, and commissions, with accompanying compensation, should embrace a period of time long enough to enable this to be done.

A WARNING TO THE STATES

If, now, we pause for a final glance at the situation, we shall discover that an imperative duty of good faith rests upon the States. The nation, by assigning certain subject and functions to the national government, acted upon the principle that like conditions demand like laws; that, by assigning certain other subjects and functions to the state governments, the nation, with equal precision and definiteness, acted upon the principle that unlike conditions demand equally unlike laws, and that,

through the failure of the States to keep their laws in harmonious touch with the rapidly evolving uniformity of conditions that come at present within their purview, the social, commercial and industrial interests of the whole country are made to suffer by the attempted adaptation of like conditions to unlike laws. We see, furthermore, as a natural result of this anomalous condition, widespread unrest on the one hand and incoördinate efforts at remedial activity on the part of the States on the other hand, with the federal government, the natural focus of popular appeal, forced to extend its powers to the utmost limits of constitutional interpretation in an effort to protect the welfare, not alone of distinct interests, but of all the people of all the States. We see, likewise, what it requires no prophetic vision to discern; namely, that if the present assignment of powers as between the federal and the state governments shall continue as at present to annoy the people and embarrass progress, the nation, in the exercise of its sovereignty, must and will readjust these powers — let us hope, by the open and fair means of constitutional amendment rather than by the more insidious and less candid method of forced construction of the Constitution as it stands. In an effort to avoid either of these contingencies, in an effort honestly and faithfully to fulfill the obligations imposed upon them in the beginning by the nation itself, the States are obviously in need of some mechanism which, while consultative and advisory in its limitations, could still enable them to act in concert on all questions requiring uniformity of treatment. It has seemed to me that such a mechanism might be realized in a body such as I have described, and which might with propriety be designated as a Council of States.



SECOND SESSION

TUESDAY EVENING, NOVEMBER 12, 1907, 7.30 TO 10 O'CLOCK

CHAIRMAN, GOVERNOR GUILD OF MASSACHUSETTS

PROGRAM

1. INTERSTATE COMITY IN TAXATION.
Hon. Frederick N. Judson, author of "Treatise upon the Law and Practice of Taxation in Missouri," St. Louis, Mo.
2. THE ECONOMIC AND STATISTICAL VALUE OF UNIFORM STATE LAWS ON THE SUBJECT OF STATE AND LOCAL TAXATION.
L. G. Powers, Chief Statistician of Bureau of the Census, Washington, D.C.
3. OUTLINE OF A MODEL SYSTEM OF STATE AND LOCAL TAXATION.
Hon. Lawson Purdy, President of Department of Taxes and Assessments, New York City.
4. CONSTITUTIONAL LIMITATIONS AFFECTING TAXATION.
Isidor Loeb, Professor of Political Science and Public Law, University of Missouri, Columbia, Mo.
5. UNIFORM PUBLIC ACCOUNTING.
Joseph T. Tracy, Chief Deputy, Ohio State Bureau of Uniform Public Accounting, Columbus, Ohio.
6. ACCOUNTING FOR THE PROCEEDS OF ALL COLLECTIONS OF TAXES AND PUBLIC CHARGES AND DISBURSEMENTS OF EVERY KIND.
Harry B. Henderson, State Examiner of Public Accounts, Cheyenne, Wyoming.
7. DISCUSSION.

INTERSTATE COMITY IN TAXATION

BY FREDERICK N. JUDSON, LL.D.

Of the St. Louis Bar. Author of "Law and Practise of Taxation in Missouri" and the "Power of Taxation," and Chairman of the Missouri Tax Commission of 1906.

THIS subject naturally suggests itself for consideration at this Conference, as it was the one on which the National Conference on Taxation, held in Buffalo in 1901, under the auspices of the National Civic Federation, distinctly and emphatically declared itself.

This conference after a full discussion unanimously adopted the following resolution:

"Whereas, Modern industry has overstepped the bounds of any one State, and commercial interests are no longer confined to merely local interests; and,

"Whereas, The problem of just taxation cannot be solved without considering the mutual relations of contiguous States; be it

"Resolved, That this Conference recommend to the States the recognition and enforcement of the principles of interstate comity in taxation. These principles require that the same property should not be taxed at the same time by two state jurisdictions, and to this end that if the title deeds or other paper evidences of the ownership of property, or of an interest in property, are taxed, they shall be taxed at the situs of the property, and not elsewhere. These principles should also be applied to any tax upon the transfer of property in expectation of death, or by will, or under the laws regulating the distribution of property in case of intestacy."

Double or duplicate taxation is recognized as essentially unjust and an abuse of the taxing power. Our courts hold that even in the absence of an express constitutional prohibition against duplicate taxation, they will always presume against it, because it is violative of public policy and natural justice.

Thus, it was remarked by the Supreme Court of the United States in a recent case (*Buck vs. Beach*, 206 U.S. 392), in denying the right of the State of Indiana to tax notes executed in and made payable in Ohio to a resident in New York, which had been moved into Indiana for the purpose of evading taxation in Ohio, that the rule laid down by the Court tended to prevent the taxation in one State of property in the shape of debts not existing there, which, if so taxed, would make double taxation almost sure, which, said the Court, "is certainly not to be desired, and wherever possible to be prevented."

It is true that double taxation may exist through the exercise of the taxing power by a State where interstate relations are not involved. Thus, the State may tax property and the money paid for the property; land and the mortgage on the land; property and the income from the property; the capital invested in a business and the privilege of conducting the business. As a rule double taxation in the administration of the tax laws of the State is avoided by statute. Thus, the holders of shares of stock are usually exempted from taxation where the corporate property is taxed. There is an exception in the taxation of mortgages, which, in most States, are sought to be taxed as personal property in the hands of the mortgagees without any deduction to the mortgagor in the tax on his property, while in a few States mortgages are not taxed at all where the property mortgaged is taxed.

Assuming that there is no discrimination between the same class of property or persons, the power of the State to tax twice is said to be the same as the power to tax once, that is, no federal constitutional question is raised by the exercise of that power. But while duplicate taxation in the form of property taxation is, as a rule, avoided in our state taxation, and sometimes expressly prohibited by constitutional provisions, there is a widespread double or duplicate taxation resulting from the subjection of the same property value to the taxing power of two jurisdictions, as in the case where the owner of property is domiciled in one State, and the property is located in another; or where the paper evidence of property is in one State and the property itself is in another; or in cases of inheritance or succession taxation, where the decedent is domiciled

in one State, and his property located or the legatee resident in another.

Thus it was forcibly said by one of our most eminent economic authorities on taxation, Professor Seligman:

"It need not be pointed out, that amid the complexities of modern industrial life equality of taxation cannot be attained without a careful consideration of these problems. To-day a man may live in one State, may own property in a second and carry on a business in a third. He may die in one place and leave all his property in another. He may spend all his income in one town and may derive that income from property or business in another. He may carry on business in several States, or if he has invested in corporate securities, the corporation may be the creature of another State, or be situated to do business in a third. All these cases may affect foreign States or separate commonwealths of the same federal State, or separate cities or counties of the same commonwealth. The possible entanglements are well-nigh innumerable."

It may be stated in broad terms that the due process of law and the equal protection of the laws guaranteed by the federal Constitution do not enforce interstate comity in state taxation except to a very limited degree. A State cannot tax property which is not located within its jurisdiction, but it can tax, not only the property which is located within its jurisdiction, but the business which is there carried on irrespective of the domicile of the owners of the business, and under the unity and mileage rules, it may tax that part of interstate properties, both tangible and intangible, which are within the jurisdiction. It cannot within the application of these rules tax any part of such property, tangible or intangible, which is not located within the jurisdiction. The real difficulty in the application of the principle of interstate comity lies in the fact that the jurisdiction of the State for taxing purposes extends not only over property and business within its borders, but over the *persons* domiciled therein.

Thus the State, in the exercise of its power of taxation over property located in the jurisdiction and the business there conducted, may disregard the fiction that personal property has its situs at the residence of the owner, and may tax all property, even including notes, bonds and the like, though

belonging to non-residents, which can be said to have acquired an independent situs in the State. On the other hand, through its power of taxation over the persons domiciled in the State, it may insist that credits have a situs at the domicile of the holder, and require their listing by him for taxation. This was ruled in the case of *Kirtland vs. Hotchkiss*, 100 U.S. 491, where the Supreme Court of the United States held that a citizen of Connecticut was properly assessed for taxation in Connecticut on bonds owned by him, which were executed in Chicago, and secured by mortgage in Chicago, these bonds being assessed as part of his personal property. The Court said that such taxation, however unjust in an economic sense, did not violate any principle of the federal Constitution, and that it was immaterial that the debt was secured by mortgage upon the real estate in Illinois, which was presumably taxable there.

The only limitation upon this comprehensive power, which really is incident to sovereignty, is in the taxation of tangible property permanently located in another State or country. Thus, in *Union Refrg. Transit Co. vs. Kentucky*, 199 U.S. 194, the Supreme Court declared that the argument against the taxability of lands within the jurisdiction of another State applied with equal cogency to tangible personal property beyond the jurisdiction of the State. Such property was not only beyond the sovereignty of the taxing State, but did not and could not receive protection under its laws. In this case the Court declared that due process of law was denied a Kentucky corporation by a tax assessed upon its rolling stock permanently located in other States and employed there in the prosecution of its business. The Court, however, was careful in its opinion to say that the case did not involve the question of the taxation of intangible personal property, or of inheritance or succession taxes, or questions arising between different municipalities or taxing districts in the same State, which are controlled by different considerations.

On the other hand, it has been directly ruled in *Blackstone vs. Miller*, 188 U.S. 189, that interstate comity was not enforced by the federal Constitution to prevent duplicate taxation under conflicting inheritance laws of the States. Thus, in

this case it was held that the beneficiaries under the will of a non-resident could not invoke the federal Constitution to prevent duplicate taxation under the New York inheritance laws, or a transfer under such laws of debts due the decedent by a citizen of New York, though the entire inheritance was taxable in the State of the decedent's domicile.

A notable example of double taxation through the non-observance of interstate comity is illustrated by state inheritance tax laws. A State may impose a tax not only upon an inheritance by law or its own interstate laws, of the property of decedents domiciled therein, but it may also impose a tax upon the property located in its territory, which passes under the inheritance laws of any other State. The decedent may have been domiciled in one State, his personal property may be located in another, while the heir or legatee may live in a third jurisdiction.

The Supreme Court of New York said in such a case that "it was unfortunate that the laws of the different States relating to succession taxation were not uniform and framed to prevent double taxation."

Another frequently quoted case of double taxation is in the case of shares of stock or bonds of a foreign corporation, or bonds of another State, which are assets in the hands of the citizen taxable by the State wherein he is domiciled. Such securities are taxable, as a rule, not because they are specifically mentioned in the tax laws, but because they are included in the property which the individual citizen is required by law to return for taxation. Some States specifically require the enumeration of such property. Thus, the statutes of the State of Missouri provide that all notes, bonds or other evidences of debt made taxable by the laws of this State held in any State or Territory other than that in which the owner resides, shall be assessed in the county where the owner resides. This statute was amended so as to include such property after the Supreme Court of the State had held that the owner of such property was not obliged under the then existing law to list them for taxation (*State ex rel vs. Howard*, 69 Mo. 454).

The same principle was applied by the Supreme Court of the United States in the case of the exercise of the federal

power of taxation, where the Court sustained a tax levied upon a bank, though part of the capital was invested in foreign countries (*Sedgwick vs. Bank*, 114 U.S. 111). The Court said that the investment which the bank had made abroad was still the property of the bank, and a part of its capital.

The taxation of corporate shares is an interesting illustration of the necessity of the observance of interstate comity in taxation. The commercial relations of our people are not controlled by state laws; corporate securities, both stocks and bonds, are freely invested in by all our people irrespective of whether the corporation is organized under the laws of the same State or not; and few States have based this question of taxation of corporate shares upon sound economic and just principles not limited to state lines.

A notable illustration of a sound principle is the statute of Arizona, Sec. 2838 R.S.: "Shares of stock in a corporation possess no intrinsic value over and above the actual property of the corporation which they stand for and represent, and the assessment and taxation of such shares, and also of the corporate property, would be double taxation. Therefore all property belonging to corporations should be assessed and taxed, but no assessments should be made of shares of stock; nor should any holder thereof be taxed therefor."

The State of Connecticut has distinctly recognized the principle of interstate comity, and the Supreme Court of that State has said in *Lockwood vs. Weston*, 61 Conn. 211, that the legislature intended to have shares of stock in foreign corporations held by owners and residents taxed only in the exceptional cases where they were not in fact taxed elsewhere. Such, I understand, is the rule of New Hampshire and New York and also of Rhode Island and Vermont.

It has been suggested that this principle of the Connecticut statute might be applied for the enforcement of interstate comity on the retaliatory principle, by providing that such exemptions of resident stockholders, as to their holdings of stock of non-resident corporations, should only apply where the laws of the State of the incorporation provided a like exemption. This retaliatory principle has been enforced by the courts in the case of conditions of admissions of foreign

corporations to do business in the State. It was remarked by Justice Brewer, then on the Supreme Court of Kansas, 29 Kans. 672, that such provisions for the admission of foreign corporations were more properly deemed "of reciprocity than of retaliation."

In *Kidd vs. Alabama*, 188 U.S. 730, it was said that "no doubt it would be of great advantage to the country and to the individual States if principles of taxation could be agreed upon which did not conflict with each other, and a common scheme could be adopted by which taxation of substantially the same property in two jurisdictions could be avoided, but the Constitution of the United States does not go so far. The State of Alabama is not bound to make its laws harmonious in principle with those of other States."

The consequences of the general disregard of interstate comity in taxation are very much controlled by the obvious fact that, except in the case of inheritance and succession taxation, the taxation of tangible property, whether interstate or State, is practically ineffective, as in the nature of things it must be. Statutes subjecting intangible property, such as stocks and bonds, and other evidences of indebtedness, are essentially unenforceable, as it is practically impossible to enforce from the taxpayers the disclosure for taxation of such property located or secured in other jurisdictions.

The Secretary of State of the United States, in a recent address made these impressive remarks, which have been very widely discussed:

"I submit to your judgment and I desire to impress upon you with all the earnestness that I possess that there is but one way in which the States of the Union can maintain their power and authority under the conditions which are now before us, and that way is by an awakening on the part of the States to the realization of their own duties to the country at large."

These words are peculiarly applicable to the disregard by our States of the duties growing out of their membership in the American Union in the exercise of the power of taxation. Our commercial and business relations do not recognize State lines. No subject comes home more closely to our people than the

enforced contributions to the support of the governments which protect them in the enjoyment of life, property or business. The disregard by the States of their membership in the Union in the exercise of this supreme power of taxation must therefore be condemned as inconsistent with any rational conception of patriotic duty.

This subject has been considered in relation to the duplicate taxation caused by a disregard of interstate comity. In view of the suggestive remarks of the representative of the Dominion of Canada this afternoon, this view is narrow compared with the broader conception of international comity. Double taxation of property, whether induced in disregard of interstate or international comity, is alike repugnant to economic justice. We may rightfully appeal, therefore, to the universal law of mankind, the *jus gentium* of the civilians, which was said to be common to all nations because resting on the nature of things and the general sense of equity which obtains among all men, as condemning any form of double taxation through the action of conflicting jurisdictions.

THE ECONOMIC AND STATISTICAL VALUE OF UNIFORM STATE LAWS ON THE SUBJECT OF STATE AND LOCAL TAXATION

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THE economic and statistical values of any law relating to taxation are seldom identical. For this reason the topic assigned me involves two separate and distinct subjects — the *economic* and the *statistical* values of uniform state laws relating to state and local taxation. Neither of these subjects can properly be considered apart from the results of the uniform interpretation and enforcement of tax laws. They will accordingly be so considered in this paper.

The economic and statistical values of uniform tax laws are disclosed by the study and observation of their results in two or more States, while those of the uniform application of such laws may be noted in the experience of different States or in the different municipalities of the same State. In both cases the values observed consist largely in the correction of the evils which result from diverse tax laws, or the want of uniformity in their enforcement.

The economic value of the laws of any given State relating to taxation depends upon a great number of factors, among which may be mentioned the existence or non-existence of similar laws in other States. In the case of immovable property, such as lands, and movable property that is necessary for the proper utilization of farm lands, or which is employed in a few enterprises other than agriculture, the existence of different tax laws in two adjoining States does not exercise any economic influence other than the burden which those laws impose upon such property. It is quite otherwise with the greater portion of movable property other than that utilized in the cultivation or use of agricultural land. If this property is taxed in one

State and not in another, or is taxed at a higher rate, or is subject to more annoying methods of taxation in one State than in its neighbor, there arises at once a movement of such property from the State of highest taxation and of the most onerous exactions, to that of the lowest taxation and least onerous exactions. Many examples of this movement may be found in the history of American taxation — notably in that of the savings bank deposits in the New England States; another illustration of the same general character is found in the fact that many rich men change their residence from States and municipalities where all personalty is taxed, to those in which the larger portion of such property escapes taxation. When tax laws are uniform in a group of States, no such transfer of wealth is to be noted. The economic phenomena accompanying or resulting from the exercise of the taxing power are identical in all the States, and the results to be observed are determined by the general character of the laws which are in force.

Diverse interpretations of the methods of enforcing laws relating to taxation have economic results of great significance, while uniform methods of interpretation and enforcement do away with all the economic evils that follow in the case first mentioned. The character of these evils, and thus the good results that follow a change from a diverse to a uniform application of tax laws, well deserve a passing reference in this connection.

In Illinois some years ago, when the revenue laws of that State required all property to be assessed at its full market value, some counties assessed land approximately as the law required, and others for less than 10 per cent of its true value. As a result, the property owners of the counties first mentioned paid nearly ten times as great a relative portion of the state taxes as those last mentioned. Similar, though not so great, variations and unjust tax burdens may be found in the great majority of States in which the apportionment of state taxes between counties is made by the legislature or by large and cumbersome boards of state equalization, with members giving more thought to local burdens than to a careful and scientific consideration of the actual and relative wealth of the several counties. The removal of these evils has, in a few States, been measurably

lessened by the establishment of tax commissions consisting of a limited number of men trained in economic science and familiar with the use of statistics. In such States the citizens experience the beneficial results of an approximately uniform application of the general property tax for the support of the state government, including the state contribution for public schools.

Ordinarily the evils resulting from the lack of uniform application of tax laws is smaller with counties and cities than between the municipalities of the same State. An exception to this general rule is frequently — may I also say generally — to be observed in the application of the general property tax in our larger cities. In such cities a great number of men are employed in making assessments; the real property assessed is held under a great variety of conditions and is employed for a great many purposes. Unless directed by a single mind, trained in scientific and business methods, and guided by a keen sense of justice, a common law is made in such cities to levy many unjust, because unequal, burdens upon great numbers of taxpayers. Such evils can only be reduced by securing the approximately uniform application of the tax laws in all parts of the city through the use of methods allied to those now employed by the most progressive state tax commissions. .

Greater New York may be taken as an illustration of the principles set forth above. In that city, prior to the appointment of the present board of taxes and assessments, the assessors within the old city of Brooklyn reported an assessment materially lower relatively than did those of the old city of New York or the present borough of Manhattan. Here was a social and economic injustice which favored the taxpayers of one portion of the great city at the expense of those of another. Under the loose system, or want of system, of the old board of equalization, there was no way of securing uniformity, and hence no method of correcting this inequality and injustice. Since the creation of the present board of taxes and assessments — especially since the appointment of the present president of the board — great progress has been made toward uniformity of practice in all parts of the Greater New York, and thus toward the elimination of the evils of the older system.

In this connection attention is called to an economic and social result of unequal assessments that is measurably removed by the application of approximately uniform appraisement of property subject to taxation: the growth of modern cities and the development of the facilities of the great municipality tend to add to governmental expenditures faster than the increase of population or of wealth. The resulting increase of taxation is cheerfully borne, or at least is endured, by the average citizen and taxpayer with equanimity, provided he believes that his added burden is not exceptional and that all people are bearing their just share of the increasing cost of government. Under these circumstances, the increase in our public expenditures that is necessary to maintain the present efficiency of city government and to improve upon the same can readily be obtained by securing more uniform and equitable application of existing or future tax laws, and by demonstrations on the part of tax officials that their administration leads to this much-to-be-desired end.

Before passing to the second subject involved in my topic, I will say that a poor tax law, even though in universal use, leads to undesirable or even vicious results; and good economic results can follow such uniform tax laws as are here under discussion only when such laws are conceived in the spirit of equity, are the embodiment of intelligence, and take account of the economic development of the State for which they are enacted. Our fathers, in the original thirteen colonies, had nearly uniform tax laws; at least, their legislation upon the subject of taxation more nearly approximates uniformity than does the similar legislation of to-day. The old laws were fairly well adapted to the economic situation of a purely agricultural people. The changes in tax legislation which the last century has witnessed in our American commonwealth have not been introduced by reason of the existence or non-existence of uniformity in the elder legislation, but solely from the fact that due to the change of economic conditions of society the old tax laws have become inadequate. They do not tend to lay equal burdens upon all classes, but to promote inequality in such burdens. To remove such inequality there has arisen in the States, with many large cities, and with great corporate wealth,

a need of departing from the earlier uniformity. The existence of this Conference bears testimony to this fact. The many delegates here assembled have been drawn hither mainly by reason of the fact that tax legislation based upon the older uniformity has become inadequate. You are here assembled to discuss the subject of taxation because you recognize that tax laws, to be just, must be so framed as to consider all the complex conditions in modern civilization. The legislator and economist, in their studies concerning tax laws, should therefore place the idea of equity before that of uniformity, and the adaptation of laws to social conditions before agreement with the laws of any other State.

The statistical value of state laws relating to state and local taxation depends very largely upon their uniform enforcement. With such enforcement, or without exact and definite information concerning the variations due to differences in such enforcement, statistics relating to taxation are worse than useless; they are mischievous and misleading. No individual who desires to be called a statistician is willing to arrange data relating to the assessment or collection of taxes and say that the resulting tables accurately disclose the relative burden of revenue laws in different States and communities. His studies on the subject tend constantly to give him information of local customs which modify all statistical tables. Thus, the United States Census Office, in testing its statistics of farm acreage, disclosed the fact that in a number of New York counties the farm acreage exceeded the acreage of all land assessed as acre property. It ascertained that in Montgomery County the national and State census of farm acreage for fifty years had been substantially unchanged, and was from 5 to 7 per cent greater than the corresponding acreage of land assessed for taxation. The variation was found to have arisen from the fact that the local assessors, in reporting acreage, made deductions for road areas, areas covered by the beds of rivers, and areas which by reason of the presence of rocks and swamps had no value. These deductions were not authorized by law, but merely resulted from local customs that had been in existence for more than sixty years. No record was kept of these deductions in any township. The local assessors, by them, sought to secure an equalization

with other towns within the same county, and yet the county board of supervisors, sitting as a board of equalization of assessment, equalized farm values without regard to this prior adjustment. In Otsego County a similar deduction was made in the northern half but not in the southern half. Some six other counties had deductions such as has been here described for a part or a whole of the territory. The state board of equalization — or the tax commission — equalized values for the several counties for the distribution of state taxes, and took no account of the fact that the acreage of these counties had been artificially reduced nearly 10 per cent, while the tax data of the majority of the counties gave the acreage without any similar reduction.

Again, the Census Office, in its studies of national wealth, discovered that in a State with one of the most efficient tax commissions, the published estimates of the true value of taxed real property were for some counties less than the census report of the value of farm property. One of these counties had a village population of nearly fifteen thousand, and had considerable investments in manufacturing establishments, in addition to the store buildings and residences of those domiciled in the villages. Other counties in the same State were shown by the same reports with an assessed valuation of real property that approximated the census value of farms and factories and also allowed liberally for all other forms of real property. As a result of this difference in assessment, the county above mentioned practically escaped taxation on property of the value of all its village houses, stores, and factories.

Another illustration, though of lesser economic significance, was met with in Iowa. A law of that State enacted in 1874 authorized the assessors to make deductions for the value of road areas included in the deeds of farm land. The state auditor, in his instructions to the county auditor, has each spring for thirty years given directions for carrying out this provision of law. A critical study of the state auditor's report for 1900 raised the suspicion that this provision of law was not observed by all the counties in the State. Letters to the county auditors relating to the subject elicited the reply from over a dozen that no deduction was made in their counties for road areas, and that there was no law authorizing such deductions. Ignorance of

these auditors — which was inexcusable in the face of the printed instructions which they had received from the state auditor — added about 2 per cent to the state tax of the citizens of their counties. The fact marks at once the difficulty of securing uniform application of even the simplest and most explicit of tax laws, and the consequent difficulty of using statistics of public taxation without a reasonable margin of uncertainty due to the lack of uniform methods of enforcing tax laws.

I call your attention to these facts to emphasize the conviction that has been growing in my mind for a number of years, that the subject of the enforcement or application of tax laws is one demanding as great consideration as that of the character of the laws themselves. I am glad to know that this conference is to discuss a variety of methods and schemes of taxation, but I wish in this connection to add that none of these schemes or methods are self-operative. If enacted into law, they are to be enforced by fallible men acting as public officials; if left to themselves, without the guidance of some one familiar with the subject, these officials will soon be giving different interpretations to the statutes and confusion will arise as in the case of existing laws. I mention this fact, not as an argument against any proposed scheme of taxation, but to emphasize the need of intelligence and vigilance in the enforcement of our tax laws, lest they lead to social and economic inequalities and make the statistics based upon the operation of such law of little or no value.

OUTLINE OF A MODEL SYSTEM OF STATE AND LOCAL TAXATION

BY LAWSON PURDY

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New York

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INTRODUCTION

SYSTEMS of taxation are not made to order, but grow out of the history and environment of the people. Changes are generally the result of new habits of life, new methods of business, new forms of property and general modifications of environment. Any consideration of a model tax law adapted to all the States must be governed by the fact that no two States

have precisely the same history, or law or conditions. All that can properly be attempted is such an outline as may readily be adaptable to the conditions in any State. In the following outline every State will find something already in force, and the elastic character of the system proposed allows easy modification and change, as conditions and habits of thought may change.

It is beyond the bounds of possibility that the wisdom of the present shall suffice for succeeding generations. One of the best features any tax system can have is susceptibility to easy modification and one of the worst is a condition of crystallization.

CONSTITUTIONS

The constitutions of the older States as originally adopted contained few provisions in regard to taxation. The constitution of the State of New York was absolutely silent on the subject until 1901, when an amendment was adopted prohibiting exemption of real or personal property by private or local bill. The constitutions of Massachusetts, Connecticut and Pennsylvania contain almost nothing to limit the power of the legislature. All of those States have profited by this freedom from constitutional restraint.

The federal Constitution prohibits discrimination between subjects of the same class, and between residents and non-residents; it prohibits interference with interstate commerce. These constitutional guarantees afford ample protection to the citizen. Further restraints upon the power of the legislature are efforts to impose the will of a living generation upon all those that are to come.

The constitution of Ohio provides that: "Laws shall be passed taxing by a uniform rule all moneys, credits, investments in bonds, stocks, joint stock companies or otherwise; and also all real and personal property according to its true value in money." The evils of such restraints have become very apparent in all States which, like Ohio and others of the West, have legislated by constitution. These evils will grow worse and worse as the conditions of modern civilization become still more complex. Minnesota has amended its constitution, and Washington and Missouri have amendments pending. The constitution of the new State of Oklahoma will restrain the

legislature no more than that of Minnesota. The Constitution of Minnesota was amended to provide that: "The power of taxation shall never be surrendered, suspended, or contracted away. Taxes shall be uniform upon the same class of subjects and shall be levied and collected for public purposes." The same amendment is pending in the State of Washington. This is vastly better than the former restrictions, but needs the following modification, "within the territorial limits of the authority levying the tax," which should be added so that the sentence may read, "Taxes shall be uniform upon the same class of subjects within the territorial limits of the authority levying the tax."

To legislate by constitution is to legislate for the benefit of courts and lawyers and against the interests of the people. The constitution should furnish a skeleton of government and not a code of laws.

DIVORCE OF STATE FROM LOCAL TAXATION

Until about twenty-five years ago, the main reliance for state revenue was upon the general property tax. Property was assessed locally by local assessors and a tax imposed on such assessments for state and county purposes, as well as for city or town and other local purposes. Many years ago it was apparent that this was a bad plan, because local assessors were induced to make low assessments in order to save their own localities from paying a proper share of revenue to the State. To remedy this evil, boards of equalization were established, which were supposed to supervise the work of local assessors, and to equalize and bring to a common level the assessments in every county, so that each county should contribute its proper quota of state expenses. The conditions are such that no state board can perform this duty accurately, and their work has always been severely criticised, sometimes justly, as directed by political and personal considerations.

It is inevitable that so long as the State relies upon a tax upon property as assessed by local officials, they will be influenced by the fact that their work affects the contribution of their own districts to larger political divisions. The competition between local assessors to cut down the burden of state

taxes results in assessments contrary to law at a small percentage of the true value of property, and inequalities in local assessments are sure to follow. When assessments are made at a percentage of full value gross inequalities may exist without being apparent. If, for example, the average assessment is only one half of full value, some property may be assessed at only 25 per cent of what it is worth without attracting much notice, and other property may be assessed at 75 per cent of the sum for which it would sell, without the injustice attracting the attention even of the owner. If every assessment in such a place were doubled, some property would be assessed at a great deal more than its selling value, and the injustice and inequality would immediately appear. Assessment, as the law directs, at the full value of property is absolutely essential to secure equality.

From every point of view, good government requires the divorce of state from local taxation.

Exclusive Reliance upon Special Taxes Objectionable

For the last thirty years, economists and state administrators have seen the necessity for some form of divorce of state and local taxation, and have attempted to separate the sources of revenue by providing for the needs of the State by special taxes on selected subjects, laid at unvarying rates. In a few States this effort has been so far successful that the State is wholly supported by such special taxes. Everywhere, however, evils have appeared as a result of this policy. This system admits of no elasticity. Sometimes the state revenue is excessive, when extravagance is inevitable, and sometimes it is insufficient, and the State is forced to borrow or curtail legitimate expenditures. The lack of elasticity, moreover, deprives the people of the State of any direct concern with the management of the state expenditure. Every owner of taxable property should feel a direct concern with state affairs. Extravagance of state officials or of the legislature should come home to him immediately in the increase of his tax payments. To supply the State with money by means of special taxes levied at unvarying rates does not solve the problem. Some such taxes may properly be levied, but there should always be a margin

to be levied so that the amount necessary will vitally interest every taxpayer.

Apportionment on the Basis of Local Revenue

A method of raising so much state revenue as may be required in excess of that produced by special taxes is already in operation in the State of Oregon, and has been advocated in the State of New York by such responsible bodies as the New York Tax Reform Association and the Chamber of Commerce. By this plan so much state revenue as may be required is apportioned to the several counties in proportion to the actual local revenue raised for all purposes in each county. A state board is charged with the duty of obtaining reports from every taxing district in the State, showing the amount of its revenue. Each county is required to pay to the State that proportion of the total sum to be raised which its local revenue is of the total local revenue throughout the State. If the local revenue raised by any county and all the taxing districts within it is one tenth of the total local revenue, that county would pay one tenth of the state tax.

The statistics compiled to carry out this plan of apportionment would be exceedingly valuable in themselves. The taxpayers in every county would have an interest in keeping down their local expenditures, but as those local expenditures would be very much more than the sum they would be required to pay to the State, this inducement would not operate so strongly as to lead them to curtail proper expenditures for local purposes. Every taxpayer would get a bill annually showing the quota of his county to the State and the quota of the preceding year. If the amount increased, his attention would immediately be called to it, and he would inquire whether the state expenditures had increased, or the expenditures of his own town had increased so as to increase the town's share. Every taxpayer would thus be interested in state affairs, would resist the undue extension of state functions and extravagance in conducting the business of the State. By apportioning the state burden in this manner, local assessments would no longer have any influence whatever in determining the amount of state taxes any community would pay. It would be prac-

licable and probably desirable to provide county revenues by apportionment among the smaller political divisions of the county, such as towns and cities. In this way all questions of county equalization, which are frequently as troublesome as state equalization, would be avoided.

SUBJECTS OF STATE TAXATION

The selection of proper subjects for state taxation must be governed by the history and present conditions of each State. Revenue is now derived from some States under laws which are not by any means perfect, but which have been in existence so long that it would be undesirable to change them at present. In some cases the State should perform the work of assessment, and whether it should retain the revenue or distribute it to the cities and towns is a question which must also be solved in view of the existing conditions in the State.

The following subjects, if taxed at all, will generally be found suitable for state revenue:

- Inheritances,
- Mortgages,
- Insurance,
- Business corporations,
- Mineral rights,
- Public service corporations.

Inheritances

A tax imposed on the transfer of property at death, commonly called an inheritance tax, is becoming a common source of state revenue, and is employed by many foreign countries. There are, therefore, a large number of precedents in the form of laws which have been in existence for a number of years, and which have been construed by the courts. It is a tax which, if imposed at all, must be imposed at unvarying rates, and the proceeds must go to the State, for the complications which would arise from an attempt to enforce the tax locally would be almost insuperable. There are certain principles which should govern the drafting of an inheritance tax law, principles which are frequently disregarded.

An inheritance tax law should not offend against interstate

hazard of fire and damage of various kinds, or to insure business enterprise against hazards of almost every description.

Insurance, then, is designed to relieve the State from the support of dependents, and to keep in being property or business enterprises which contribute, in one way or another, to the support of the government. It is, therefore, generally far from a fit subject on which to impose any material part of governmental support. While it is true that insurance companies of various kinds make large profits, it is also true that any tax equally imposed on any form of insurance will ultimately be shifted to the insured by an increase in premium rates.

No tax on the business of insurance can be justified, but a tax imposed only on the surplus funds withheld from distribution would be open to less objection than a tax which would directly increase the amount of the premium charged.

Real property belonging to an insurance corporation should be assessed and taxed for local purposes only. If any tax for state purposes should be imposed, in the form of a percentage of premiums earned on contracts made within the State, the tax should be the same in form on the premiums for all kinds of insurance, whether the contracts are made by foreign or domestic corporations or individuals. All reciprocal legislation, which is really in its nature retaliatory, should be avoided; it savors of war between the States, and introduces a feature of contention injurious to the State and very adverse to the proper business of insurance.

If a state tax be levied on premiums, the personal property of insurance corporations should be exempt from local taxation.

Business Corporations

In almost every State there is some provision for a tax on business corporations for state purposes in addition to the local taxation of their real and personal property. Some States, as New Jersey, impose this tax solely upon corporations of their own creation for the privilege of incorporating under their laws. Other States, as New York, impose a tax alike on foreign and domestic corporations in proportion to the part of their capital invested in the State.

There seems no good reason for imposing any taxes on busi-

ness corporations in excess of the taxes imposed on individuals doing the same class of business. If the opportunity to incorporate is open to every one for the payment of a small fee, there is no special privilege involved, and all are equally at liberty to avail themselves of the continuous existence and freedom from personal liability obtained by corporate organization. The invention of the corporation provides conveniently for the coöperation of many people in an enterprise, all of whom cannot participate in the management. Doing business in corporate form is becoming a necessity of modern conditions, and there is no excuse for penalizing an efficient instrument.

All corporations, domestic and foreign, may properly be required to pay a small license fee to meet the cost of administration incident to their proper registry.

Mineral Rights

Mineral rights are a proper subject for state taxation, because their value does not depend upon local expenditure, or the value of local government or on the extent of local population. Deposits of coal, iron and other minerals owe their value to the demand for their use by the country as a whole. If mineral rights are taxed only for local purposes, the tax will be inadequate to induce their best use, and the locality in which they are situated will contribute too small a proportion of the state's revenue. If the State relies for part of its revenue on a tax apportioned in proportion to local revenue, towns in which there are valuable mineral rights will not contribute their share, unless such mineral rights are taxed directly by the State for state purposes.

Ordinarily a state tax on mineral rights should not be imposed upon the site value of the land, because the surface can be used for agriculture or other purposes, while mining is going on beneath the surface. In some cases the deposits of ore are so close to the surface that the operation of mining the ore is like quarrying stone. In this case it might not be possible to allow the local community to tax the site at all, and provision might be made for a division of the proceeds of a tax on the mineral rights. With the exception of such mines as are practically quarries, the tax for state purposes could be imposed

on the mineral rights alone, and the local tax districts could be allowed to tax the surface for local purposes.

Such a tax on mineral rights should be imposed whenever possible, upon the capital value, excluding the value of the surface. If, for any reason, this is not practicable, the tax can be imposed in the form of a royalty.

Public Service Corporations

The real estate of public service corporations not used in the operation of the service should be taxable locally for local purposes. Any tax in addition to the local tax should be assessed by a state authority by mathematical rules so that the necessity for judgment on the part of assessors shall be eliminated.

Public service corporations should be so dealt with as to secure the best service at the lowest cost to users, and the plan of taxation should be so devised that it may be easy to reduce taxes as the charges for service are reduced. When the accounts of public service corporations are kept as public accounts, and their net earnings are limited by the reduction of charges to a reasonable return upon the actual capital invested, any tax will be a tax upon the users of the service. So long as charges for service are unlimited by law, or charges are permitted greatly in excess of the cost of rendering the service, the power of taxation may properly be used to recover for the public part of the monopoly value due to the liberality of the franchise.

In most of the American States the taxation of railroads and other public service corporations had its beginning in the general property tax. This was soon found defective, and in some States has been abandoned altogether, in others supplemented by new forms of taxation, while in a few states at least railroads were never subjected to the general property tax, but were taxed from the beginning by special systems devised for the purpose.

State Railroad Commissioners condemn General Property Tax

In 1878 the convention of State Railroad Commissioners appointed a special committee, consisting of Charles Francis

Adams of Massachusetts, W. B. Williams of Michigan and J. H. Oberly of Illinois, to examine and report as to the methods of taxation as respects railroads and railroad securities then in vogue in the various States of the Union, as well as in the various counties, and to report a plan for an equitable and uniform system for such taxation. These commissioners issued a circular and interrogatories in relation to the matter, which was sent to all the state executives, to a large number of railroad corporations and to a number of foreign countries. The replies are printed in full as part of the report of the committee, and a compendium of the system in use in all the States of the Union was prepared. In their reports the Committee said: "The conclusions reached by the committee as a result of their investigations can be very briefly stated. The requisites of a correct system of railroad as of other taxation are that it should, so far as it is possible, be simple, fixed, proportionate, easily ascertainable and susceptible of ready levy. . . . The conclusion at which your committee arrived was that all the requisites of a sound system were found in taxes on real property and on gross receipts, and in no others." The committee proposed that the real estate outside of the right of way should be locally assessed exactly in the same way as other real estate. Beyond that a certain fixed percentage should be assessed on the entire earnings of the corporation, and this should be in lieu of all forms of taxation upon the property of the corporation and upon its securities. The entire burden should be imposed in one lump on the corporation, and levied directly. The committee proposed that when a railroad is only in part in one State the tax should be apportioned in proportion to mileage.

The committee discussed various forms of taxation and condemned the law of Massachusetts as it then was and said:

"Clumsy and devoid of scientific merit as it unquestionably is, however, the Massachusetts system would seem to be preferable to that still in use in New York, concerning which the State assessors, in their annual report for 1873, expressed the opinion that under it there was no uniform rule for any road in any county, each assessor being governed entirely by his own views. In certain towns the railroads appear to pay about one third

of the entire taxes, while the assessed valuation in 1878 varied from \$400 per mile to \$100 per rod. The difference in the assessment of the New York Central and Hudson River road, where for all purposes that the road can be used it is of the same value to the company, is \$24,000 per mile. In short, it is scarcely an exaggeration to say that the assessments are as unlike as the complexion, temperament and disposition of the assessors. It does not need to be pointed out that a system such as this, and it is the system in most general use, compels the corporations in self-defence to an active participation in local politics. Indeed, it is not too much to say that as a system it is open to almost every conceivable objection."

The New York system, which is so severely condemned, remains unchanged to this day, though supplemented by other taxes. One railroad in the State of New York, which has by no means the largest mileage, pays more than 1900 separate tax bills every year, and all the railroads have constant trouble with local assessments, and are obliged to keep track of an enormous number. This is an obvious waste of effort and source of demoralization.

Gross Earnings Tax Unjust

Professor Edwin R. A. Seligman, in his work on "The Taxation of Corporations," speaks of the inadequacy and practical failure of the general property tax. He speaks of the general property tax as applied to railroad and other public service corporations as primitive, unequal and furnishing an incentive to dishonesty. The only system now in use in any American State which he commends is that employed in Connecticut, that is, measuring the tax by the market value of the stock plus the indebtedness in the proportion that the mileage in the State bears to the total mileage, the assessment of course being made by one single board. Professor Seligman makes a very strong and I think conclusive argument against the gross earnings tax as economically unsound and legally invalid. He speaks of the report of the Railroad Tax Commission, from which I have already quoted, with much respect, but says of the gross earnings tax which they recommend, that while it possesses many undeniable advantages, it has a fatal defect. "It is not proportional to the real earning capacity, it takes

no account of cost, nor does it pay regard to the expenses which may be necessary and just. . . . Of two corporations which have equally large receipts, one may be in a naturally disadvantageous position which increases unduly the cost of operation or management. Clearly its ability to pay is less than that of the rival company in possession of natural advantages." Professor Seligman argues in favor of a net receipts tax, but recognizes that there are certain dangers connected with this plan.

A New Method proposed for the Taxation of Public Service Corporations

I think that all the objections that can be raised against the net receipts tax can be obviated by imposing the tax in a similar manner to the United States internal revenue law of 1864. The tax was imposed on all dividends and all interest. In framing such a law for the use of any State it would be necessary to use all dividends and interest simply as a measure of the tax. The tax could not be imposed directly upon the dividends and the interest, or we should meet the same difficulty as that experienced by Pennsylvania in its attempt to tax foreign-held bonds. This difficulty is entirely met by using the dividends and interest on indebtedness simply as the measure of the tax upon the corporate property within the State. For the purpose of illustration I have made a computation from the data contained in the report of the New York Railroad Commission, and I find that the total taxes of all kinds paid in all States by the steam surface railroads reporting to the Railroad Commission in the State of New York amount to slightly less than 15 per cent of the total disbursements of these roads on account of interest and dividends. When the property of a railroad or other public service corporation is situated in more than one State, the tax must be apportioned on the mileage basis now in common use.

If the tax on dividends and interest were exclusive, it might be objected that if there were no dividends and interest there would be no tax at all. To obviate this objection it would be proper to impose a very small tax on gross earnings, not exceeding, for example, 2 per cent. So long as the tax on gross

earnings exceeded the tax on dividends and interest, the latter should be omitted, and as soon as the tax on dividends and interest exceeded the gross earnings tax, the tax on gross earnings should be discontinued.

In the case of a public service of an interstate character, the tax on gross earnings can only be imposed upon the earnings arising from business done within the State.

Let us briefly consider some of the advantages of this manner of taxing all public service corporations.

If the tax on all the corporate property is measured by the dividends and interest paid, the corporation has only one assessing board to deal with, and that assessing board has purely ministerial functions to perform. It ascertains the amount of interest and dividends paid, a matter which cannot be concealed, and performs a simple sum in multiplication. The corporation knows exactly what tax it will be obliged to pay, it has no interest in the personnel of the board that does the assessing, because no dispute can arise as to the amount of the tax.

When a new corporation starts its tax will be light. If it earns neither interest nor dividends, it will pay only the small tax on gross earnings, and the tax should be small, because it is rendering a public service at cost. If it earns interest and dividends for those who contributed the capital, in proportion as it pays them it must pay taxes to the State. In prosperous years its taxes will rise and in lean years will fall automatically.

It may be objected that if a railroad or other public service corporation becomes bankrupt, the tax will be very small; but this is an advantage, not a disadvantage, for it is for the public interest that a corporation in such condition should be rehabilitated as soon as possible, and the automatic reduction of taxation will operate to that end. As soon as it earns enough to pay investors, the tax will increase. It may be objected that a corporation could refrain from paying dividends and accumulate a large surplus. This, again, is rather an advantage than an objection, for in the long run its accumulated surplus will enable it to perform better service, pay larger dividends, and in consequence heavier taxes.

From every point of view and in accordance with the testimony

of all experienced observers with whose writings I am familiar, it is clear that all public service corporations should be taxed as a unit, and it seems self-evident that discretion on the part of assessors should, if possible, be eliminated. I have suggested a method already tried and found effective, by which the assessment can be made without judicial discretion.

The proper disposition of taxes imposed on public service corporations remains for consideration, and to a great extent the answer must conform to the conditions now existing in each State. In some States the major part of taxes on some or all of the public service corporations is retained by the State; in others, State revenue from this source is small. As a general principle it is wise for the State to retain a large part of the taxes on public service corporations which own their own right of way, and to distribute to the localities in which the public service is performed the taxes on those corporations which use the streets and public places. The street-using corporations owe the value of their property to the extent and character of the population and government of the communities in which the service is rendered. The cost of their protection is mainly a local charge. The distribution of the taxes paid by such corporations is a comparatively simple matter, because they frequently own property in no more than one taxing district.

The case of steam railroads is very different. The value of their property very largely depends upon terminals, and it is impossible to assign a definite portion of the value of their property as a whole to any particular section of it. Communities without a single mile of railroad track contribute largely to the value of the corporation's property, and no local distribution of the taxes can compensate such communities. It seems, therefore, that the State may properly retain a large part of the revenue from railroads and other public service corporations which make little use of streets and public places, so that all the communities in the State may share in the revenue.

When taxes on public service corporations are distributed to the localities in which the service is rendered, a fair and practical measure of the distribution is to apportion the tax in proportion to the length of the railroad track, or the pipes, wires or the like

in each tax district. In the case of steam railroads, the apportionment should be based on the total length of tracks, including branches, sidings and switches, so that terminals and large cities may receive a fair proportion. Even on this basis rural districts will be somewhat favored.

ELASTICITY ESSENTIAL

It must not be forgotten that a considerable part of state revenue should be apportioned to the local tax districts in proportion to local revenue, and raised by direct taxation. It is not only unnecessary but very undesirable to obtain all state revenue from the special taxes imposed on subjects of state taxation.

The legislature must at every session be obliged to fix an amount of money to be raised locally by direct taxation. This is essential that the people may control the legislature, restrain extravagance and limit the extension of state functions.

SUBJECTS OF LOCAL TAXATION

If the power of the State to tax is limited to the subjects previously described, all other subjects will be left to the jurisdiction of the local authorities. The following subjects are generally taxable locally:

- Licenses imposed pursuant to the police power,
- Business licenses, if any,
- Banks and trust companies,
- Personal property, not taxed by the State,
- Real estate,
- Revenue from public service corporations.

Licenses imposed Pursuant to the Police Power

The most important source of revenue from licenses is from the licenses for the sale of liquor. It would be beyond the scope of this paper to make suggestions in regard to the amount of such licenses, but it seems obvious that whatever the amount may be it should be retained by the local community. It is common for local communities to have the power to prohibit the sale of liquor altogether, and it is certainly unfair that a community in which no revenue is derived at all from the sale of liquor

should share in the receipts obtained in other communities. If the State takes any part of such receipts and expends them for general state purposes, every community in the State receives the benefit of a fund to which some communities do not contribute.

Business Licenses, if Any

Certain business may properly be licensed for purposes of police regulation, but business licenses should not be imposed for revenue. If they are so imposed, the local communities should retain the proceeds, for it is the local communities that protect the property and render the business profitable.

Banks and Trust Companies

The power of the State to tax banks being limited by federal statute, the field of discussion is narrowed. National banks cannot be taxed at a greater rate than other moneyed capital, and it seems only proper that the taxation of other moneyed capital should not be at a greater rate than the taxation of national banks, and, so far as practicable, should be identical in manner as well as rate. The decisions of the courts as to what is moneyed capital have placed trust companies in the same class as banks, and have excluded almost every other corporation. For practical purposes, then, we can consider banks and trust companies as members of the same class and the only members of that class.

In the experience of New York and other States a law requiring the assessment of bank shares at market value is very unequally enforced. When the rate of taxation is the same as the ordinary local rate, there is a very great difference between both the rate of taxation and the assessment of banks located in different towns but otherwise similarly situated.

It is unfair and improper that any person or corporation as a stockholder of a bank should receive a bonus by special exemption, or by deducting indebtedness from the value of the shares owned. Any tax should be on the book value of all shares alike, and should be paid by the bank. Under these circumstances a much lower rate than the average local rate will generally yield as much revenue as the usual form of assess-

to exempt from taxation any class of property, or to reduce the assessment upon any class of property, it would be possible for any progressive community to adopt methods already proven valuable elsewhere, or to make experiments on its account which would be useful object lessons to the rest of the country.

The policy of Pennsylvania has already demonstrated the great advantage of exempting certain classes of capital used in manufacturing, and of imposing a low rate of taxation on certain classes of securities. In Baltimore, Md., the rate of taxation imposed on securities was greatly reduced, and the revenue largely increased. In some States certain agricultural improvements are exempt, and the exemption has been very beneficial. It is universal experience that manufacturing machinery is most difficult to assess, and local power to exempt is frequently exercised in States where this power is enjoyed.

This local option would give power to those most deeply interested, and who have the best opportunity to judge of the facts. The exercise of the power could have no ill effect on any other community in the State.

With a complete divorce of state from local taxation, and a large measure of local self-government accorded to local communities, we may confidently expect a continuous and rapid advance toward an equitable system of taxation, which will aid and encourage agriculture, commerce and manufacturing, promote the general welfare and finally equalize natural opportunities.

CONSTITUTIONAL LIMITATIONS AFFECTING TAXATION

BY ISIDOR LOEB

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As is indicated by its title, this paper will deal with the legal and political rather than the economic phases of the problem of taxation. Many of the other papers which are to be presented at this Conference will doubtless touch upon the constitutional aspects of the tax reforms which are advocated. It is desirable, however, that special consideration should be given to this subject because in most of the States it is of fundamental importance to the entire question of the reformation of the methods of taxation.

Mr. Purdy has just presented an admirable outline of a Model System of State and Local Taxation. It is a safe assertion, however, that before this plan could be introduced into the majority of our States radical amendments of the constitutions would be necessary. Mr. Purdy himself has stated that "the constitutions of at least twenty-four States contain limitations upon the power of the legislature which render impossible the adoption of any sensible system of taxation." Tax commissions appointed to recommend changes in taxation have voiced the conclusion that the first and essential step in tax reform must take the direction of modification of existing constitutional provisions. The recent report of the Missouri Tax Commission contains the following language: "The legislature is so hedged about and hemmed in by the limitations in the fundamental law of the State, that, as the constitution stands, no statutory change can be made in the general taxing system now in force. In other words, . . . nothing short of a constitutional change, either by a new constitution or a constitutional amendment, can open the door to the establishment of any other

system." The California Commission in its report of 1906 takes substantially the same position.

Additional evidence of the existing condition is afforded by the numerous constitutional amendments affecting taxation which are proposed by state legislatures. It is evident that an understanding of the general nature of these constitutional limitations and of the causes which have led to their adoption is an essential prerequisite to the introduction of reforms in the tax system. Legislation which is framed without regard for such provisions will fail, as the courts have shown that they will strictly construe the limitations imposed by the constitution in this regard.

This paper will be confined to a consideration of the limitations affecting taxation which are to be found in state constitutions. These provisions represent a phase of the general movement which has resulted in the establishment of numerous restrictions upon state legislatures.

Originally, as is well known, there were comparatively few limitations upon legislative power in American state constitutions. The latter were brief documents which embraced matters of a strictly fundamental character and excluded detailed provisions, which were left to be provided by the legislature. From the beginning there was a tendency to expand the constitution, but this did not manifest itself in any marked degree until about the middle of the nineteenth century. Since that time the movement has been a rapid one, and to-day, with the exception of a few States, chiefly in the northeastern section of the country, the constitutions are voluminous pamphlets dealing with many matters which formerly had been left to be regulated by statute. In addition to the positive legislation contained in the constitution there are numerous provisions, commanding, prohibiting, or restricting legislative action with regard to a wide variety of matters. That this tendency is still manifesting itself is shown by the fact that the constitutions which have been most recently adopted are much longer and more detailed in character than any which have preceded them. While the average American constitution contains less than twenty thousand words, those of Virginia and Oklahoma embrace more than double this number.

Distrust, on the part of the people, of their representatives in the legislature constitutes the most general explanation of this development. This lack of confidence was in part justified by acts of the legislatures, but much of it was due to the development of democratic ideas of popular sovereignty and direct legislation. Convinced of the merits of a particular measure, the people hastened to incorporate it into the constitution, where it would be free from legislative modification. As we shall see presently, this attitude, which betrayed a lack of historical intelligence, had much influence in fastening the general property tax system upon the majority of American commonwealths.

While the restrictions upon the financial powers of the legislature are merely a part of the general mass of constitutional limitations, they were the first to appear, and represent the most stringent division of such provisions. This was natural in view of the fact that anything which touches the purse acquires particular importance. In addition, however, a special cause for this condition existed in the financial policies which had been pursued by some of the States. In order to promote the construction of railroads, state and local aid was granted to an extensive degree and under a variety of forms. While in some cases the public interests were safeguarded, a combination of fraud, extravagance and financial depression left many communities facing large debts and heavy tax rates. In many instances the railroads were not constructed, and there was no increase in land values to compensate the taxpayer for the burden which was imposed upon him. As a result the demand arose for constitutional limitations which would prevent the state and local governments from aiding or engaging in economic enterprises. The restrictions which were adopted to meet this demand would prevent a recurrence of the evil, but they were not sufficient to satisfy the people, who insisted that their officials and representatives should be deprived of the power of incurring debts or imposing high rates of taxation for any purpose. Connected with this was the demand for the prohibition of all privileges and exemptions in taxation such as had been granted to railroad and other corporations. As a result the constitutional limitations in many States were extended

so as to apply to the subjects and rates of taxation, to exemptions and to public indebtedness. The new States which had not passed through a financial experience of this character followed the practice of the older States when they framed their constitutions. In this way the stringent tax limitations which were inserted in the Missouri constitution of 1875 found their way into the constitutions of other States.

The constitutional provisions which apply to the subjects of taxation were due for the most part to the desire to prevent any one from escaping his just share of the burden of taxation. The people wished to establish equality and uniformity in this respect, and, lacking an intelligent appreciation of the principles of taxation, it was natural that they should conclude that this could be best secured by subjecting all objects of property to the tax.

Hence constitutional provisions were framed and adopted, providing, as in Indiana, that "The General Assembly shall provide by law for a uniform and equal rate of assessment and taxation; and shall prescribe such regulations as shall secure a just valuation for taxation of all property, both real and personal." In order to make assurance doubly sure sections were frequently included which prohibited all exemptions of property from taxation except a minimum amount in favor of educational, charitable and similar interests. Other provisions required specifically the taxation of the property of railroad and other corporations. It will be shown by other speakers that even if these provisions could have been perfectly carried out they would have failed to realize equality and uniformity in taxation. But their adequate enforcement was impossible in the absence of an efficient administration. With the ineffective machinery provided under our local government system, the actual conditions of taxation became just the opposite of those intended. Inequality and lack of uniformity became characteristic features and were accompanied by contempt for the law and disregard for the sanctity of an oath.

While the constitutional limitations have thus failed to secure the end desired, they nevertheless remain as serious obstacles to tax reform. Separation of the sources of state and local revenue, local option in taxation, and, in many States, equitable corpora-

tion taxes became impossible because of such provisions. The courts have indicated by their decisions that relief cannot be expected from that quarter. Indeed, in some cases they have increased the difficulties of the situation. Thus, for example, a court which upheld an inheritance tax on the ground that it was not a tax on property, nevertheless strongly intimated that any exemption based upon the value of the inheritance would be in conflict with the constitutional prohibition upon exemptions of property from taxation. It is probable that this court would take the same attitude regarding progressive rates in inheritance taxes where the constitution requires that taxation of property shall be equal and uniform.

Constitutional provisions affecting the rate of taxation are of chief importance, however, in connection with limitations upon maximum rates for state and local purposes. It has been indicated that in some States the people were so alarmed at the excessive rates necessary to meet the obligations which had been incurred that they secured the adoption of constitutional provisions prohibiting the levy of a rate beyond a certain amount which was fixed in the constitution. Undoubtedly some limitation upon the rate of taxation was necessary, but the methods adopted were, in many cases, arbitrary and irrational. A good illustration is afforded by the provision for reducing the maximum rate when the total assessed valuation exceeded a certain figure. This was based upon the fallacy that the expenses of the State would not grow as rapidly as its taxable wealth. Moreover, the reduction required in the rate was in some cases so great that the total revenue under the new rate was necessarily much smaller, notwithstanding the increase in assessed valuation. Thus, in one State, the Board of Equalization was compelled for several years to keep the total assessed valuation below the amount named in the constitution, as otherwise the lower rate of taxation which would have been necessary would have resulted in a serious deficit in the revenues of the State. Idaho, whose constitution contained a provision of this character, adopted an amendment in 1906 repealing the requirement.

The constitutions generally provide that rates fixed for special purposes can be increased to a certain degree by a vote

of the people, but for other purposes the maximum fixed cannot be exceeded under any circumstances. This frequently works a hardship upon local governments, particularly cities which are unable to raise sufficient revenue with this rate. It is true that the valuation of property can be increased, but here injustice results under a system which does not provide for a separation of the sources of state and local revenue, as the municipality will be compelled to contribute an undue proportion of the state revenue. Notwithstanding this fact, the paradoxical situation is often presented of a community protesting against the reduction of its assessed valuation by the State Board of Equalization. The latter wishes to make the ratio between assessed valuation and real value the same as in other counties, but the local authorities respond that under the limited tax rate this would cause a deficit in local revenues and, rather than face such a condition, they prefer to pay an additional amount into the state treasury.

The fact that these and other constitutional limitations are producing inconvenience and hardship in the several States is clearly shown by numerous efforts to secure their modification. Independent of the character of the restrictions, the fact that the constitution embraces detailed provisions would of itself necessitate frequent amendment. As these provisions are not of a fundamental character they partake of the nature of legislative acts. As such, while they may be suited to the conditions under which they were enacted, changes in wealth, population and social and economic conditions in general will necessitate modification from time to time as in the case of statutory revision. Some idea of the extent of this movement can be gathered from the statistics of the proposed amendments to constitutions which have been submitted to the voters for their ratification or rejection. A table prepared by Professor John B. Phillips shows that in the eight years from 1895 to 1902 inclusive, two hundred and eighty-one separate constitutional amendments were voted upon by the people. Of these, one hundred and sixty-eight were adopted. Large as these figures are, they are exceeded by those of subsequent years, which prove that the movement is increasing rather than diminishing in extent.

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The statistics for the last four years are as follows:

YEAR	ADOPTED	REJECTED	TOTAL
1903	12	14	26
1904	42	32	74
1905	17	4	21
1906	46	24	70
Total	117	74	191

A comparison of the two periods, 1895-1902 and 1903-1906, shows that the average number of amendments voted upon in each year increased from thirty-five in the first period to forty-eight in the second, while the average number of amendments adopted increased from twenty-one in the former to twenty-nine in the latter.

A large proportion of these amendments apply to the financial provisions of state constitutions and indicate the dissatisfaction produced by the existing constitutional limitations. The remedy which is sought in this manner betrays in some instances a complete misunderstanding of the operation of constitutional provisions. The amendment, by providing in detail for the reform desired, frequently accentuates the evil by introducing further restrictions. It is in fact much as if an inebriate should endeavor to reform through the use of some of the alcoholic patent medicines. The real difficulty exists in the restriction itself and this cannot be corrected by the introduction of new limitations.

The articles on taxation and revenue in state constitutions have been constructed with such careful reference to the limitation of legislative power that an amendment of one section inevitably affects several other provisions. This difficulty cannot always be overcome by proposing amendments to the different sections involved as one or more may be rejected while the others are ratified. The situation may best be remedied by the adoption of a comprehensive amendment repealing the article on taxation and revenue, and substituting in place thereof provisions of a more rational character. But care must be taken to avoid too great detail in such revision. The plan pro-

posed by the California Tax Commission is open to criticism in this respect. The draft amendment submitted by the commission, while providing a system of taxation which is obviously superior to the one it proposes to displace, in parts, descends into much greater detail than the existing article, and if adopted, the demand for further revision must inevitably arise. It does not follow, of course, that the plan advocated by the commission was not the most expedient, but this in itself would illustrate the general condition produced by the prevailing attitude toward constitutional limitations.

The rational plan should take the direction of removing most of the restrictions which state constitutions impose upon the taxing powers of legislatures. This would not lead to the exploitation of individuals or corporations, as the principles of individual liberty which have been incorporated into the Constitution of the United States are a sufficient guarantee against discriminating and confiscatory taxation. Moreover, restrictions upon special legislation would be retained. Nor does it follow that all restrictions upon the rates of taxation and financial operations of local governments would disappear. So long as the legislature must act through general laws it may be trusted with the determination of the maximum rate, which can be raised to meet new conditions as they arise. In addition to this, an administrative control may be developed which can extend its supervision over the general financial operations of local governments.

It may be that the time is not ripe for the seemingly radical remedies which have been proposed. It has been indicated that there is little evidence of a tendency to remove the constitutional limitations upon legislative action. But it may be noted that we have at least taken some step in the direction of substituting efficient administrative supervision for control by legal definition. It is coming to be recognized that administration is more important than legislation. Railroad and tax commissions composed of experts are doing missionary work in this field. Administrative bodies of this character must be more and more relied upon in the solution of the complex problem of the equitable distribution of taxation, a solution which constitutional limitations have hindered more than they have advanced.

GOVERNOR GUILD: I am sorry to announce that Mr. Harry B. Henderson, the State Examiner of Public Accounts of Wyoming, cannot be with us, but we are very fortunate in having present to-night one who is thoroughly competent to speak upon this important subject and who will make a short statement — Mr. Joseph T. Tracy, Chief Deputy of the Ohio State Bureau of Uniform Public Accounting.

UNIFORM PUBLIC ACCOUNTING

MR. TRACY:

Mr. Chairman and Gentlemen of the Conference:

Mr. Foote informed me yesterday evening that Mr. Henderson could not be present, and asked me to say a few words upon the subject of "Uniform Public Accounting." I have met Mr. Henderson many times in our national associations and have been greatly profited by hearing his experience as to his work in Wyoming. While his work there has not the scope and authority that we are given in our department in Ohio, still his experience of fifteen or twenty years in public accounting has been of great assistance to the members of those meetings engaged in that work.

Gentlemen, I shall not take up much of your time. I have nothing prepared to read to this assembly, and it is not necessary to inform people of the experience in public affairs of this Conference, those composing this meeting, or to bring to you arguments in favor of the value of uniform public accounting.

The Ohio law, passed in 1902, created or organized a department consisting of three deputies, with the auditor of state as chief inspector and supervisor, charging them with the duty of prescribing and formulating an accounting system to be installed in all public offices of the State, including municipalities, cities and villages, counties, school districts and townships. We have installed systems of accounting in nearly all public offices with what degree of success the people of Ohio are generally informed or familiar with. Our work also extends to the inspection of public offices by state examiners who are trained in the knowledge of the law and in the application of law to the

affairs of the various public offices. The supervision of public offices is an important feature of our work. A man going into a new office, perhaps unfamiliar with its duties and anxious to follow the law and to obey this supervision, can be given almost invaluable assistance by our department. These men going into office, who want to start right at the beginning of their tenure of office, look to our department for aid, and these calls have, in fact, been more than could be taken care of by our force of examiners.

Now, the main object of my presence upon the platform here to-night is to notify you that at the last meeting of the National Association of City Comptrollers, a committee was appointed to draft a model uniform public accounting law. This committee was appointed last September and is now engaged in gathering data for such a model law for such supervision, and to those of you who are interested in that subject or the adjudication of that subject, I would state that this committee expects to report about the first of January and will give reasons why we believe there is the greatest value to the public in such State inspection and supervision. This report will be made to the officers of the national association, and if this Conference or the National Tax Association desires copies of that report, as a member of that committee I will state that it will afford us pleasure to place that report, embodying both the law and the reasons therefor as given by the committee for the enactment of such a law, in the hands of your representatives. (*Applause.*)

ACCOUNTING FOR THE PROCEEDS OF ALL COLLECTIONS OF TAXES AND PUBLIC CHARGES AND DISBURSEMENTS OF EVERY KIND

BY HENRY B. HENDERSON

State Examiner of Public Accounts, Cheyenne, Wyo.

THE discussion and line of thought of this Conference will be largely confined to uniformity in laws for assessment of properties, the kind of properties to be assessed, the basis of valuation and how the valuation shall be determined. It will also consider the levying of taxes, upon what properties, tangible and intangible, taxes shall be imposed, and to what purposes indirect taxes ought by right to be applied. If uniformity is desirable in these particular matters, then is it not equally important that there should be uniformity in accounting for the proceeds of the levies made from year to year?

In the first place, I believe it is an acknowledged rule of law that no tax shall be levied except in pursuance of law, and every law imposing a tax shall state distinctly the object of the same, to which only it shall be applied. The purpose for which a tax is levied must necessarily be stated, and this purpose must be carried to the treasurer's cash, where the entry of the collection of the tax is made. Moreover, the application of the funds must be safeguarded. There must be no juggling of accounts. There must not be authority vested in any one whereby the funds which have been levied can be diverted to some other purpose than that named in the original levy. If such a matter is permissible, then the object for which the tax was levied would only serve as a subterfuge for the purpose of raising revenue that might be used for any purpose the council, the commissioners or the State might determine upon.

The receipt of moneys from all sources should be credited on ledger accounts under the respective headings for which the levies have been made. No other method of accounting for

receipts would be admitted as being reasonable or legal. I know, however, that my contention in this respect will not meet with uniform approval. There are those who believe tax levying bodies ought to be empowered to make levies and create a revenue which may be diverted at will by the disbursing officers — that a transfer from one fund to another where the purpose is for the betterment of local conditions is not a violation of the statute. Much as I respect the judgment of those who will so contend, and the spirit which oftentimes brings action of this kind to be adopted by governing bodies, yet I submit that it is an irregular procedure, contrary to the best interests of the governed; and while the funds may not be dissipated in the true sense of the word, yet they are dissipated in not having been used for the purpose for which they were created. Tax levies at the time they are authorized are passed upon a valuation already ascertained by a method of assessment. The aggregate levy for the respective purposes is a matter of computation. At the time the tax list is turned over to the treasurer or collecting officer, he should be charged by the state, county or municipal comptroller, auditor or clerk, with the aggregate amount of the tax and the aggregate amount to be credited to each of the respective funds for which the levy was made. This charge should stand against the treasurer or collecting officer, subject, however, to credits to be made at the close of each month for such collections as have been made and properly reported to the comptroller. He should be responsible for the entire amount save and except wherein he is unable to make collections by reason of there being no tangible property available to levy upon. The treasurer should make return of the tax list, or tax warrant as it is frequently termed, within a specified period of time. He should show the aggregate collections under such tax list, the credits spread to the respective funds, the aggregate amount uncollected, and the aggregate amount that would accrue to the respective funds if such collection were made. He should make upon such return a showing to the tax-levying body, or other proper officers having authority, why unpaid taxes are so returned, and he should be relieved only when it is shown beyond any question of doubt that every possible effort has been exercised to make such collection. With a showing of this character

the tax-levying officers or such other officer as may be delegated for that purpose should have authority to authorize a credit to be entered in favor of the treasurer upon the comptroller's records for all amounts uncollected which it seems were impossible of collection. The residue of the unpaid tax, whatever it may be, should be made a liability against the Treasurer and his bondsmen, and its payment not only required, but its collection enforced forthwith. In this manner the tax list of the year is adjusted within a limited number of months, and the collecting officer is enabled to make full returns and thus remove the office completely from political domination. We all know that there are influences exerted in every community that are not healthful for the financial interests in so far as they pertain to the collection and disbursement of public funds. If the collecting officer knows that there is no avenue of escape by reason of neglect of duty, there is not a question of doubt as to his exercising every method of procedure placed at his command whereby such collection can be made.

It will be urged that the levying of tax for specific purposes is not to the best interests of the governed. In other words, that the revenue derived cannot be expended to as great advantage as if the levy was made *in solido* and the appropriations for specific purposes made from the revenue thus created. I agree with the contention that a tax levy for every specific matter in public government would be unwieldy and burdensome, but for special purposes a specific levy should be made and never be diverted from the purpose for which it was levied. The general fund is recognized as one from which all disbursements are to be made for general purposes, and from this fund specific appropriations are made and constitute a separate credit upon the accounting officer's records. These appropriations are chargeable with every disbursement for the purpose named in the appropriation and none other. The comptroller is the only one who can regulate a matter of this character, and even he can be deceived if an untrue account is returned for payment. Padded accounts or false vouchers are the lowest kind of graft and eventually will result in shame, dishonor and disgrace. Appropriations if honestly handled will be expended only for the purposes named in the act creating them. Public officers

have suggested that when the purpose for which a specific appropriation had been made was accomplished, there is no reason why the residue of the appropriation might not be transferred by the accounting officers to other appropriations in which there was an apparent deficiency. Indeed, this policy has been insisted upon by some very brilliant men. While we have confidence in the accounting officers, yet the adoption of such a plan would resolve itself into a lack of control by the governing bodies. For example, if legislative appropriations could be so juggled by the accounting officers, what would be the ultimate result? Surely nothing but scandal could follow, and the same rule would apply down the line throughout the various government organizations.

I maintain that the disbursements of public funds are of a necessity to be more closely scrutinized and considered in the matter of accounting than the receipts. There is no particular danger arising from distribution of funds. That is a matter very largely of computation, but when it comes to disbursement of these funds, there are so many avenues down which the stream of expense may run that it is oftentimes difficult to keep in mind the relationship of the appropriation, whether by levy or otherwise, and the expenditure. Once the classification is lost sight of, then chaos immediately comes in and rules. If the accounts are not uniform, if there is no uniformity in the regulation of the public service, then the revenues are subject to dissipation through diversion to such an extent as to make the public service a subject of contempt.

The National Tax Association, through the able men who are now directing its affairs, and those who will become associated in its administration and membership, has it within its power to devise ways and means of assessment and taxation that will be of untold benefit to the people at large. Indeed, I am not sure that you realize how great a service you may perform.

I am confident that the general manifestation of interest in the subject of public accounting and the purpose of the National Comptrollers and Accounting Officers Association, will do much toward providing safeguards in the accounting departments for all receipts and disbursements. At a recent meeting of the Association last named, the lack of uniform laws respecting the

examination and supervision of accounts was a noticeable feature in the discussions, and indeed very few States had any laws whatsoever governing this important matter. The Association passed a resolution providing for a committee to prepare a bill that would be uniform in its general character, to be urged before legislative bodies for consideration and enactment. We hope to have the good offices of the members of this Conference in this undertaking.

The Census Bureau took up this live question for consideration a few years since and called practical accountants to its aid in preparing a schedule for the reporting of all receipts and disbursements by the several divisions of government. The present schedule is in general use and commends itself to all interested in proper classification. It will be improved from time to time as experience dictates.

The whole subject resolves itself into the proper charges and disbursements as they are directed by the individuals not identified with the accounting officers, who by reason of their position have the privilege of creating expenses that may be classified to suit their convenience. This is the main difficulty, I foresee, but it has existed at all times past, and it will be at least one step removed when the accounting officers have agreed upon a uniform system throughout the United States for every division of government. The accounting officers are the stewards of the public finance, and in the measure of fidelity that their service is performed, just in that degree will the government have risen to greater respect among the people.

A uniform system of accounting and reporting is the demand in various industrial business enterprises, and we are told that the best results obtain where the accounts are so kept as to enable an intelligent analysis of the interests involved. If such procedure is essential in the business affairs of the industrial world, it is equally essential in administering the great affairs of every branch of our government.

Uniform assessment laws, a uniform basis of valuation, uniform methods of taxation, uniform methods of accounting, business integrity and common honesty in the administration of public affairs will do much to correct existing evils.

GOVERNOR GUILD: The meeting is now open for any questions that any gentleman present may desire to ask, or for any remarks or any discussion. The meeting is now open for that purpose.

MR. ELSON (Ohio University, Athens, Ohio): Mr. Chairman, I would like to ask Mr. Purdy to explain why he thinks, as stated in his paper, that mortgages should not be taxed.

MR. PURDY (New York): It comes a little outside the line of my paper to-night. My reasons for believing that mortgages should not be taxed are several. If any tax is imposed uniformly on all mortgages, the effect of such a tax will be to raise the rate of interest on the mortgage by an amount equal to, or in excess of, the tax, thereby imposing an additional burden upon the borrower of money upon mortgage security. It seems to me obviously unfair that those who own incumbered real property should pay more taxes, or should pay more than those who own real property which is free. (*Applause.*)

MR. MATTHEWS (Attorney Ohio Tax League, Ohio): I would like to ask Mr. Purdy in what way the model tax system which he has stated or expounded to us will provide revenue sufficient to correct the evils, the greatest evils now — that is, in what way, or to what extent, it will require property other than real estate to stand its fair share of the burdens of taxation.

MR. PURDY (New York): In the subjects which I have suggested there will be found fit subjects for state taxation. We have a class of property, the main value of which is real property, but that is commonly distinguished in current conversation as free real property; that is to say, the property of public service corporations. If the gentleman from Ohio means to include in real property the property of public service corporations, then I am quite free to say I have not suggested any means of revenue which is not now derived by some State in the Union. At the same time there are certain sources of revenue that I have suggested which are not fully put in force

in any State in the Union. The main purpose, however, of taxing such a source as public service corporations is not so much revenue as to secure the best service and to enhance the value of property to such a degree that its owners can well afford to share that enhancement of value with the State.

MR. JUDY (Darke County, Ohio): As an outsider, not a member of this Association, may I say a word?

GOVERNOR GUILD: We will be very glad to hear the gentleman.

MR. JUDY (Darke County, Ohio): I have been wondering what reason the gentleman from New York could assign that people would give the true 20 per cent value of their holdings, when they would not give the true value of all their holdings. In referring to the law, I understood him to say that when they gave 20 per cent of their holdings it was satisfactory. I have been wondering what the theory was by which they could arrive at 20 per cent of the value and yet not give the true value.

GOVERNOR GUILD: I think it was the gentleman from Washington, and not the gentleman from New York, who made that statement.

MR. POWERS (Washington): I think the gentleman misunderstood me, because I did not advocate any such change as that. I simply called attention to the fact that Illinois has made that basis. Now, I think the whole thing grew out of this state of affairs in Illinois: The people did not want to give Chicago and some other places the power derived from such increased taxation and revenue as would result, which they could have had under the old tax rate. If they had raised the amount of taxes to their full value, Chicago would have four times the amount of revenue that it has to-day, which would give it added power and would thus lift it out of its difficulties, and one party fearing that the other out in Illinois would get a little more benefit from such increased revenue, thus restricted the assessment for that reason, and I think that that had more to do with it than any idea of economic equity, or making any more just tax conditions.

GOVERNOR GUILD: In the discussion, the Chair trusts that the gentlemen present will not simply confine themselves to

questions called out by the papers submitted, but will discuss any subject along the lines of taxation that may be of interest.

A DELEGATE (Massachusetts): I want to say a word, as a lawyer, with regard to one or two cases in the United States Supreme Court bearing on the question of double taxation. Of course, we all know there is no objection in the United States Constitution to double taxation, or treble taxation, or even quadruple taxation; but at the same time the Supreme Court of the United States have expressed themselves strongly against double taxation, and have said that it should be avoided in every way possible. The first case I refer to is that of *Blackstone against Miller*, 188 United States, 189, which was a case where the act of the New York Comptroller in taxing the deposits of an Illinois citizen was sustained, though the estate had to pay similar taxes in Illinois. It is generally referred to as an approval by the Supreme Court of the principle of double taxation. That case went on the ground that it was not a tax on property at all; it went purely on the inheritance tax question. They said that money or other credits being in New York, proceedings were necessary in New York to pass succession; that is, under the New York law there must be proceedings there before a person holding in New York could safely pay it over to the Illinois executor. Justice Holmes, who frames many good sentences, terms it a special succession, and says there is no objection to taxing both general and special succession, and it was upon that very narrow ground that the decision was sustained.

In a later case, dealing with the law governing this question, Judge Brown lays down as a principle that the taxes are to be collected for the public good and for the needs of the public, the State, the municipality or the county, as it may be, and he added that all attempts to double taxation are to be avoided. It is distinctly stated in that latter case that so far as tangible personal property is concerned its situs for taxation is where the property is, and it does not follow the individual. The Court goes on to say with regard to intangible property that because it is difficult to fix its situs, therefore, in property of that kind the situs will follow the individual. The Court

does not give its approval to double taxation on corporate property, first, where the corporation is, then on the stockholders where the stock is. I submit that decision is a strong dictum to the effect that such taxation would be absolutely improper. I submit it is clear upon these cases that the true principle is that a corporation should pay the tax on the property and that there should be no double taxation on the stock in the hands of individuals in another State.

MR. MCPHERSON (Georgia): May I be permitted to ask a question of Mr. Purdy? I should like to ask him why he omitted the income tax entirely from his list of the suitable sources of state revenue.

MR. PURDY (New York): It is always a great pleasure to be questioned; I only fear I may tire this audience. Answering the gentleman from Georgia, I will say I omitted the income tax because I refer to income tax as entirely unsuitable for state revenue. It is practicable, in my judgment, constitutional objections aside, to use the income tax for federal revenue. The tendency of it is to tax income at its source — the very essence of it is to tax income at its source. That means that in every corporation which pays interest on debt, and dividends on its stocks, you must retain a percentage of the dividends and the interest and turn it over to the State. I need not elaborate on the methods of reaching income at source, or the points in the case of the corporation. Four fifths, or above, of the revenue from the proposed income tax comes from the income tax reached at the source. It does not depend in the slightest degree upon the good faith of the recipient of the income. You subject the income to the tax before it reaches him. The point of that tax that is reached is the schedule, where they require statements to be made by the recipient of the income. It is impossible from the nature of our state jurisdiction to levy state income taxes at source. I do not think I need describe why.

MR. RIDDLE (Columbus, Ohio): I am an outsider, but I have been very much interested in all that has been said here to-night, and I would like to ask a question. Mr. Purdy spoke very favorably of the inheritance tax, and in favor of a very low tax upon insurance. I would like to ask him if he would

treat insurance, an insurance policy, insurance falling to any person, as an inheritance.

MR. PURDY (New York): I am inclined to think that it might very properly be treated as an inheritance, being governed by the fact that a certain sum would be exempt from the inheritance tax, so that small inheritances of insurance would be exempt altogether, and then any graduation of inheritances would be in accordance with the amount of the individual bequests; further, that the tax on collateral inheritances would be much heavier than the tax on succession. Normally, insurance would be received by the descendant of the insured; it would be a succession, not a collateral, and the tax might be very small. I should be quite willing myself to exempt it altogether, but I do not see that the line of division is very clear. Men sometimes leave very large insurances to swell already very large estates, and I see no particular reason why they should be exempted.

THIRD SESSION

WEDNESDAY FORENOON, NOVEMBER 13, 1907, 9 TO 12.30 O'CLOCK

CHAIRMAN, GOVERNOR DAWSON OF WEST VIRGINIA

PROGRAM

1. CENTRALIZED TAX ADMINISTRATION IN MINNESOTA AND WISCONSIN.
Dr. Raymond V. Phelan, Department of Economics,
University of Minnesota, Minneapolis, Minn.
2. HOME RULE IN TAXATION.
Solomon Wolff, member Louisiana State Tax Commission,
New Orleans, La.
3. LIMITATIONS OF THE PURPOSES FOR WHICH TAXES MAY BE LEVIED.
Professor Isaac A. Loos, School of Political and Social
Science, State University of Iowa, Iowa City, Ia.
4. METHODS OF ASSESSMENT AS APPLIED TO SEVERAL CLASSES
OF SUBJECTS.
James E. Boyle, Professor of Economics and Political
Science, State University of North Dakota, Grand
Forks, N.D.
5. HABITATION TAX.
Professor John B. Phillips, University of Colorado,
Boulder, Colo.
6. THE UTAH MORTGAGE TAX.
Professor George Coray, University of Utah, Salt Lake
City, Utah.
7. DISCUSSION.

CENTRALIZED TAX ADMINISTRATION IN MINNESOTA AND WISCONSIN

DR. RAYMOND V. PHELAN

Department of Economics, University of Minnesota, Minneapolis,
Minn.

It is the purpose of this brief paper to call attention to the excellent work already accomplished by the recently created Minnesota Tax Commission, and to point out, in Wisconsin taxation, two lines of development that in the opinion of the writer will find their logical conclusion in that much-desired goal, expert assessments. These two States of the Middle West afford, in their tax commissions, most noteworthy examples of scientific, public-spirited, efficient state administration, as opposed to the too frequent administration along lines of party politics. One of the arguments against the proposal for a permanent tax commission in Minnesota, was that it would be made up of politicians; but when the Democratic Governor, Johnson, transmitted to the Minnesota senate his nominations for the new tax commission, the strongly Republican Senate resolved, amid applause and by a rising vote, to confirm the nominations, and the Republican House gave expression by resolution to hearty commendation of the Governor for making such appointments, so far removed from political influence. And it may be observed in this connection that the general argument against state-administered *ad valorem* taxes on public service corporations loses some of its weight when applied to Wisconsin, for in the Badger State the administration of such taxes is in the hands of men who make a business, not of politics, but of taxation.

The Minnesota Commission has been in existence but six months, having been organized April 29, 1907. This Commission may be said to be a result of a general feeling of dissatisfaction with the tax system of the State, which has developed rapidly from a simple agricultural community to one

of varied industries, including iron mining on a large scale, lumbering, quarrying and general manufacturing. In consequence of this general feeling of dissatisfaction, especially with the administration of the personal property tax, the Minnesota legislature, in 1901, made provision for a temporary tax commission, which was to draw up a tax code, including a provision for a permanent commission. The code submitted by the special commission met with general disapproval and was rejected as a special session of the legislature in 1902. There were in the code provisions that aroused the opposition of certain special interests, and there were also provisions that awakened opposition in the farming class. By the constitution the legislature was much restricted in the matter of classifying property for purposes of taxation; but by 1906 the process of popular education along the line of taxation improvement had proceeded far enough to secure a constitutional amendment that admits of a free classification of property for taxation purposes. The legislature was thus given a free hand in the matter of taxation, and it is said in the State that this explains why the special interests did not oppose the creation of a permanent tax commission in 1907. It was a choice with them between tax legislation emanating directly from the legislature, and tax legislation guided and directed by an expert commission, and they were inclined, it is said, to prefer the latter.

Minnesota's permanent tax commission was provided for by an act approved April 25, 1907. The members, three in number, are appointed by the Governor, with the advice and consent of the senate. The first appointments were for two, four, and six years; subsequent appointments will be for six years. The Commission is to be non-partisan; not more than two of its members shall belong to the same political party, and all three must be persons known to possess a knowledge of taxation and taxing laws. The Commissioners are expressly forbidden to hold any other public office or to take an active part in any political campaign. Each Commissioner receives an annual salary of \$4500, while the total annual appropriation for the Commission is \$30,000, an inadequate sum. In the selection of the chairman of the Commission, Governor Johnson gave expression to the very encouraging spirit of coöperation,

so evident in many quarters, between the university and state administration. Dr. Frank L. McVey, for many years professor of political economy in the University of Minnesota, is the first chairman of the new Commission. The other members, Senator Samuel Lord and Judge C. M. Hall, are very distinguished and exceedingly capable men, well qualified for their work as commissioners of taxation.

The powers granted to the Commission give a great centralizing tendency to tax administration in Minnesota. The Commission is authorized and required to exercise a general supervision over all taxation in the State, and over all officers and boards having to do with tax administration. The Commission may order a reassessment of either real or personal property, or both, in any assessment district when in its judgment such a reassessment is advisable or necessary to the end that property shall be assessed in compliance with the law. It is one of the duties of the Commission to give instructions to the assessors of the various counties at meetings to be called at the several county seats. One or more of the Commissioners is required to visit at least half of the counties annually, and every county is to be visited at least once in two years, to the end that the methods of local taxing authorities may be made to conform to law. It is part of the Commission's duty also to institute legal proceedings against persons or corporations guilty of noncompliance with the tax laws, and to make proper complaints against boards of review and taxing officers. County attorneys are required to assist the Commission in its work of regulation. The Commission has full power to require of local taxing officers full information concerning their work, and to compel individuals and corporations to furnish to the Commission such information respecting their property and business as the law requires for taxation purposes. Witnesses may be summoned by the Commission and required to give testimony, or produce books, papers or records bearing upon any matter of taxation under authorized investigation by the Commission.

The Commission takes up the work of state equalization, subject to review by the State Board of Equalization, up to January 31, 1909, when the Board goes out of existence. The

Commission has authority to equalize, not only among counties and assessment districts, but also among individuals and corporations. It has authority also to order reassessments when any considerable amount of property has been illegally omitted from the assessment rolls or grossly underassessed. The Commission has thus very great control of the tax system of the State, and its control will be considerably increased if certain of its plans receive legislative sanction.

The work of the Commission will be greatly facilitated by its wise provision for a taxation library, which is being gathered and being put on a working basis by the Commission's own librarian, a young lady trained in Dr. McCarthy's splendid legislative reference library at Madison, Wis. Undoubtedly, some of the great things that Dr. McCarthy has done for general legislation in Wisconsin, the Commission's librarian will do for tax legislation in Minnesota.

Without doubt the most significant service that the Commission has rendered in its short existence of six months is in its reassessment of iron ore properties, which in Minnesota are taxed on the general property tax basis. The Commission has raised the valuation of such properties from sixty-nine to one hundred and ninety millions, which is 40 per cent of the real value as estimated by the Commission. Forty per cent is regarded as a fair average of the ratio of assessed to true value in the State. In its reassessment of the iron ore properties, the Minnesota Commission has proceeded in a most comprehensive and intelligent way, and has evolved a classification of such properties that is both new and admirable. Lands in the ore belt of the State the Commission has classified as *operating mines*, *prospects* and *iron lands*. Further sub-classifications have been made with reference to the difficulty of mining, character of the ore, character of mining rights. Taking into account these various elements affecting the value of the ore in the ground, the Commission has divided operating mines into six classes, and prospects into three classes, applying a different rate per ton to each class. Very elaborate statistics relating to the mines have been gathered. The Commission has gone very deeply into the study of iron mining, and has required elaborate reports from owners and operators. Be-

sides, the Commission, accompanied by the State Inspector of Mines, spent two weeks inspecting mining property, taking careful notes and locating each property on a map.

The other problems upon which the Commission has begun to work are those of underassessment of realty, evasion of the personal property tax, and also of the capitalization tax on general corporations. From the county auditors have been gathered complete returns for the whole State of taxable personalty as returned by the assessors. By comparing this data in specific instances with commercial agency reports and otherwise, the Commission will probably be able to effect an improvement in the assessment of personal property. In its work of determining the degree of underassessment of realty, the Commission is using the familiar method of comparing sale prices of real estate with the corresponding assessment figures. Three counties have been worked up for six years; in the other counties, two months in each of six years are being taken. In estimating the amount of this work, it should be noted that in Minnesota, real estate is assessed once in two years. The results of this real property investigation will undoubtedly be known this calendar year. The writer is very much impressed by the very heavy administrative duties of the Commission, a large part of whose time, it should be noted, is taken up with abatements.

In its short career of six months, the Minnesota Tax Commission has made a splendid start and there can be little doubt that Minnesota's system of centralized tax administration will soon attract general and favorable attention.

In the neighboring State of Wisconsin, from which the young Commission of Minnesota has received many valuable suggestions, taxation has shown in recent years two significant lines of development that in the opinion of the writer lead logically to the displacement of the old system of locally elected assessors by a system of assessors appointed by the State Tax Commission, and dependent for continuance in office not on political patronage, but on honest, efficient service. One of these lines of development has been the rapid extension of the state administered *ad valorem* system to public service corporations; the other has been a marked tendency toward complete cen-

tralized, state control of local taxation. An entirely satisfactory administration of the Wisconsin *ad valorem* system calls for expert assessments; the tendency toward complete centralized control gives great promise of the realization of such a system of assessments.

In Wisconsin, up to 1899, the general method of taxing public service corporations was on the basis of gross receipts. The gross receipts tax on railroads was in the beginning at a flat rate; later at graduated and progressive rates. The Wisconsin gross receipts system had its origin in 1854 in the desire both to do away with the inequalities of locally assessed *ad valorem* taxes on railroads, and to promote railway construction by low taxes on such agencies of progress. The financial history of Wisconsin shows an almost continuous agitation against the gross receipts tax on railroads, concerning the constitutionality of which in that State there is some doubt; but the strenuous opposition of the railroad companies prevented an abandonment of the tax until as a part of the La Follette reforms it was obliged to give way to a state administered *ad valorem* system. The change in Wisconsin to the *ad valorem* system as applied to public service corporations began in 1899, when that enterprising and progressive State declared express companies taxable on an *ad valorem* basis, which is Wisconsin's per mileage share of the value of a company's capital stock, less the value of its real estate situated outside of Wisconsin, and its personal property not used in the carrying on of the express business. The rate is the average rate on the general property in the State, determined by dividing the total taxes, state, county and local,¹ on the general property in the State by the aggregate value of such property subject to taxation. In the same year, freight line companies, companies furnishing cars to shippers, dining, buffet, chair, parlor, palace and sleeping car companies, were made taxable on practically the same *ad valorem* basis, and at the same rate. In 1903 the *ad valorem* system was extended to railroads, and in 1905 to all other public service corporations, except telephone companies, which are still taxed on the gross receipts basis. Beginning with the year 1907, telegraph companies come under the *ad valorem* system;

¹ Poll taxes and special assessments are not included.

street railways and electric lighting companies beginning with the year 1908.

A very serious, perhaps the chief difficulty in administering the Wisconsin *ad valorem* system lies in the fact that the general property of the State, contrary to law, is not assessed at its full value. Most of the real estate is under-assessed, while most of the personal property escapes altogether. In so far as realty is concerned, the chief source of correction of assessed values employed by the Tax Commission has been the records of real estate transfers, reported by the county registers of deeds. A comparison of prices at which property appears to have been sold with the assessed values of the same pieces of property, affords a rough idea of the degree of under-assessment. The returns of the registers are not, however, thoroughly reliable. Padding to increase fees, mistakes and sometimes neglect upon the part of registers, fictitious considerations in deeds, trade considerations and other factors have contributed to make the returns untrustworthy. The Commission, through Professor T. S. Adams and a considerable corps of special agents, has been able to determine the probable coefficient of error in the returns of the registers, but it cannot be denied that faulty and illegal assessments are standing in the way of a thoroughly satisfactory administration of the *ad valorem* taxes on public service corporations. The *ad valorem* system demands expert local assessments. The Commission is, it should be noted however, making every effort to administer the corporation taxes justly and equitably. In its report of this year, the Commission recommended that it be allowed to gather the statistics of real estate sales through its own agents. This will work some improvement and will further centralize the work of tax administration in the State.

The efforts of the Commission in the direction of a thoroughly satisfactory administration of the corporation taxes are encouraged by the other line of development already adverted to,—the tendency toward a completely centralized control of local taxation, a tendency that promises to give Wisconsin local assessments by trained, skilled assessors, who will be dependent for continuance in office not on political patronage or party graft, but on honest, efficient service. In 1899, largely as a result of

the fight against the railroad gross receipts tax, there was created for ten years a Wisconsin Tax Commission which was to have a general supervision of taxation throughout the State; a permanent Commission was provided for in 1905. Several laws have been enacted extending the power of the Commission. In 1901 provision was made for county supervisors of assessments, which officers, though elected by their respective county boards, are in the discharge of their duties as supervisors of the work of assessors and boards of review under the supervision and direction of the State Tax Commission, which by this same law of 1901 was given direction and control of local assessors. The county supervisors of assessments have done much in Wisconsin to improve tax administration.

Another stride in the direction of complete centralized control was taken in 1905, when the legislature empowered the Tax Commission to reassess local property whenever complaint has been entered that a local assessment has not been made in substantial conformity with the law, and the Commission is satisfied from a summary hearing that such is the case, and that the public interest would be subserved by a reassessment. When its judgment is such, the Commission is empowered and obliged by this law of 1905 to appoint and authorize one or more persons to make such reassessment and to appoint three persons to review the same. The officers of the county in which the assessment district concerned is situated are under legal obligations to lend all necessary and possible assistance to the State officers in their work, the expenses of which are borne by the district affected. Under this law the Commission in 1906 made reassessments of six different districts, which reassessments seem to have been much more satisfactory than the original assessments. In each case the reassessment resulted in a very material increase in the valuation of the property in the aggregate and also in great changes in the relative valuations placed upon the property of individuals.

Another law of the same year making an extension of central authority over local taxation, provides that on the appeal of any town, city or village in a county from the apportionment of taxes by its county board, the Tax Commission shall, if it deems the appeal justifiable, review and determine the value of all

the property in the county. The Commission is now having its first experience under this statute in the work of revaluing the personal property of two of the counties. In cases under these two laws the Commission selects its own agents and it has endeavored to select men entirely independent of local sentiment and experienced in the matter of valuations.

Thus the Wisconsin Tax Commission is clothed with authority to make amends for, and prevent injustice in, taxation, both as between persons and between local administrative units. This Commission, made up of conscientious, progressive men, has with the help of the county supervisors brought about great improvement in the tax administrations of the State, but the Wisconsin system is still far from being perfect. Even when tax laws are as just as possible, and are honestly and efficiently administered, justice can be but approximated, because assessments are liable to the fallibility of human judgment. When, therefore, the laws are not administered with strict honesty, when assessments are made by men elected by the people whom they assess, and sometimes if not often by men having personal interests and private ends that their public office can be used to promote, there is bound to be much injustice, bearing with great weight in most cases on the socially weak. There is much truth in the plaint of a poor woman who wrote to an agent of the Wisconsin Tax Commission as follows: "it seems that the Poor that have got Mortgages on thar property ar taxed mor then it is worth the Rich if thay ar taxed for six thousand git it Redused to fourthousand that is not Rite."

Those not socially weak may in some cases suffer. In one thriving and progressive city in Wisconsin the assessors were interested in the business of fire insurance. Persons who insured their property with the assessors got low assessments; those who did not were assessed high. Prominent and substantial citizens, as well as others, have told the writer that such was a fact. These assessors used their public office for private gain. Those property owners who refused to be coerced by these unscrupulous public officers paid a penalty in high assessments. Property in some cases was assessed for more than the owner was offering to sell it for. Great inequality of assessments obtained in that city. It would seem that such rascally insurance agent

assessors might be turned out of office at the first election. However, they held office for more than a dozen years, and a year before they were finally ousted it was said that they could not be beaten at the polls.

Even a centralized system such as Wisconsin's needs to be crowned with expert assessors, devoting all their time to the work of assessments, making a profession of taxation; depending for continuance in office upon honest and efficient service. The question has been raised in Wisconsin whether a law providing for appointment by the Tax Commission of assessors for local communities would be in harmony with the constitutional provisions for local self-government. The Constitution may possibly stand in the way, but Wisconsin's system of *ad valorem* taxes on public service corporations demands expert local assessments, and the marked tendency toward centralized tax administration in that State gives great promise that ere long perhaps such assessments may be a reality in Wisconsin.

HOME RULE IN TAXATION

BY SOLOMON WOLFF

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I

WITH, perhaps, a few exceptions, the constitutions of all the States of the Union contain declarations, embodying the idea that all property shall be taxed, and the tax shall be equal and uniform. Nor is this thought a thing of yesterday, for we find it in the earliest constitutions adopted by the various States.

To make these solemn constitutional declarations effective, the legislatures of the various States have, since their existence, enacted numberless lengthy and complicated statutes, providing in detail for the discovery and equal and uniform valuation of all kinds of property. Severe penalties have been provided for the punishment of those who fail to disclose property which they own, and which should be taxed. The courts of all the States have in innumerable decisions interpreted these statutes, and upheld the right of the legislatures to tax everything in sight and out of sight, so long as it had any value at all, and they have upheld the right of the legislatures to even subject property to double taxation. Here and there, an act or part of an act has been declared void as being in conflict with the constitution of a State or of the United States, but, as a whole, the legislatures seem to have unbounded power to enact legislation to make effective the constitutional declarations.

And they have made use of the power. The existing laws on the subject contain many ingenious devices for the discovery of property that unwilling owners would like to avoid having taxed. All who are suspected of being the owners of property, or of pernicious activity in accumulating property in the pursuit of a profession or a trade or commerce, are required to solemnly swear to the truth of the many inquisitorial questions which are put to them, and lustily do they swear.

Notwithstanding all these acts of the legislature, notwithstanding all the decisions of the courts, notwithstanding all the inquisitorial interrogatories, notwithstanding all the penalties and, sad to say, notwithstanding all the solemn oaths, it is a fact, well known to all who have paid the slightest attention to the subject, that taxes are not equal and uniform between different kinds of property, nor are they equal and uniform between different owners of the same kinds of property.

The reports of many investigating commissions, appointed in different States, have shown these conditions to exist, and any doubt, which we might have had, has been removed by the investigations of the federal government.

In the Census Bureau publication entitled "Wealth and Taxation," at p. 41, the true value of all the real estate, of what, since we have become a world power, is called Continental United States, is given at \$62,341,472,627, while the assessed value of the same kind of property, for purposes of taxation, is given at \$30,089,818,672, that is, only 48.26 per cent of the real estate is assessed for taxation. The true value of what is classed in the publication as "personal and other property" is given at \$44,762,719,783, while the assessed value of the same kind of property, for purposes of taxation, is given at \$8,873,562,448, that is, only 19.86 per cent of that kind of property is taxed. The inequality is glaring; real estate is assessed nearly 50 per cent of its true value for purposes of taxation, while personal and other property escapes with an assessment of not quite 20 per cent. In other words, real estate, under the present system and at the same rate of taxation, pays about two and one half times as much taxes as other kinds of property.

This inequality, between real estate and other kinds of property, is not the only inequality which obtains, for there is great inequality between different owners of real estate.

In 1892 Congress appointed a select committee to investigate tax assessments in the District of Columbia. After a searching inquiry, the committee, among other things, said (Report No. 1469, 52d Congress, 1st Session, at p. 6), in referring to several large and influential property holders: "These gentlemen, it will be seen, agree with all the other evidence taken by your committee, and with the facts which were stated by the Com-

missioners of the District . . . in declaring that all assessments, made in the District for years past, have been viciously defective in bearing with undue severity upon the poorer class of taxpayers, and unduly favoring the rich. They hold that these defects inhere in the nature of the assessment, which, in attempting to arrive at the true cash value of all property, imposes a task manifestly impossible; the attempt to do this necessarily results in the proportionate greater assessment of the small homestead than of the large and costly building."

Other commissions have come to like conclusions, and even slight reflection will demonstrate the inherent truth of these conclusions. Any reasonably intelligent man, with a little knowledge of the subject, can estimate with some degree of correctness the value of the laborer's cottage, or of the modest dwelling costing, say, \$5000; but where will you find the assessor who can tell how much it costs to erect a modern office building, a great hotel, or other like structure? Do you think that the men who usually fill the office of assessor — and I say nothing against their intelligence and integrity — have the capacity to value the palatial residences of the wealthy? The result is that moderately priced pieces of real estate are assessed at a greater proportion of their true value than the more expensive and valuable pieces.

Still greater is the discrepancy between the assessment of real estate and certain kinds of personal property.

Under the classification, adopted in the work already mentioned, personal property includes railways, telegraph and telephone systems, privately owned waterworks and privately owned electric light and power systems; it covers also merchandise, household goods, cattle and, last, it covers bond, stocks, money and credits of all kind. The term "personal property," as used here, includes everything but land and buildings; it covers tangible and intangible property; it covers the property which the assessor can see, and it covers property he cannot see. All personal, tangible property the assessor can see, and however imperfect and unequal his valuation may be, he at least has a fair chance to get it on the roll. When, however, we come to intangible personal property, like credits, stocks, bonds, notes and other like things, not only is the assessor liable to err

in valuing them, as he is with other personal property, but, more, he cannot know of the existence of most of it, unless it is voluntarily reported by the taxpayer.

The taxpayer can, however, not be relied on to make a proper return. It may be because the public conscience is, to say the least, somewhat elastic or entirely wanting when it comes to reporting property for assessment, or because there is a feeling that the prevailing system of taxation is unjust and unequal, and that, therefore, one need not scruple to make false returns; whatever the specious reasoning, by which the individual justifies himself to his own sense of honesty, the result is the same; the assessor gets about 50 per cent of the real estate, about 25 per cent of tangible personal property and about 5 per cent of intangible personal property.

Do you think I underestimate the proportion of intangible property returned? Let me give a few figures taken haphazard from various official reports.

In 1893 the net taxable credits of twenty-seven Chicago banks — that is, loans and discounts and other assets, from which are deducted all deposits and other liabilities — were, according to returns made to auditor, over one million (\$1,058,105.25); returns for assessment were \$10,000.

These same banks in the same year had taxable moneys on hand \$18,991,771.67; they returned \$43,925.

Outside of bankers, brokers, etc., all of Cook County, Ill., which includes Chicago, had but \$434,244, and the credits of all the merchants, etc., were only \$522,110.

In 1884 the total valuation of credits of bank,

banker, broker, etc., was	\$ 98,615
Credits of other than bank, banker and broker . . .	209,466
Bonds and stocks	75,830
Shares of capital stock of corporations, not of the State	100

It would be insulting to the ordinary intelligence to comment on the absurdities shown by these figures.

Nor must we conclude that this is true of Chicago or Illinois alone.

In New Jersey a commission reported in 1897, "It is now literally true in New Jersey as in other States, that the only

ones who now pay honest taxes on personal property are the estates of decedents, widows and orphans, idiots and lunatics."

In Ohio the Hon. E. A. Angell, a member of the Tax Commission appointed by Governor McKinley, said, in 1896, there was but \$1,097,283 in money returned for taxation in Hamilton County, which includes the city of Cincinnati, with nearly half a million of inhabitants. The deposits in Cleveland were about \$70,000,000; there was returned for taxation \$1,741,129.

In California the commission reported that money and credits escape taxation almost altogether.

And so it is everywhere, a little better in one, a little worse in another State. As a whole, we may fairly say of the present system that there is an entire absence of equality between different kinds of property and between different taxpayers of the same kind of property, and it is not, humanly speaking, possible to remedy this condition of things, under the present system. We may multiply statutes and decisions, increase fines and penalties and affidavits; there is no more probability of success in the future than we have had in the past. As property of all kinds becomes more varied in its character, as our conditions become more complex, as our cities become more numerous and larger, the attempt to enforce a general property tax in the manner attempted until now must — if that is possible — become less equal and less uniform, and the attempt to enforce it will continue the present annually recurring carnival of perjury.

II

The inequalities already discussed are perhaps not susceptible of correction without changes in our system of taxation far more radical than those which we are as yet prepared to adopt. There are, however, other inequalities which work great injustice, which it may be possible to remedy without any radical measures, and without abandoning the view, so widely held, that every kind of property should bear its due proportion of the necessary taxes.

Most, if not all, the States derive all or a very large proportion of their revenues from taxes imposed on every kind of property; the counties and municipalities derive their income from the same source. That is, all the property in the State, real estate and personal property of every kind, is assessed, or is sought to be assessed, and, upon the value so found, the State imposes a tax of as many mills as it may need for its purposes; then comes the county and imposes a further tax of as many mills as it may need; sometimes the municipality imposes a tax also, though here and there the county will not tax the property in the municipality, and sometimes it happens that, like New York, or in my own city of New Orleans, the municipality covers the entire county.

The assessment, which is the basis of all these property taxes, is usually made by officers in each county, and, though the State law usually provides that all property shall be assessed at its cash value, it is almost invariably the fact that one county will assess the property in its limits at a much lower per cent of its true value than another county.

To those at all acquainted with the subject, demonstration of the assertion made is not necessary, yet it is well to cite some data in support of it, and to show that this obtains, not only in one or several, but in practically all the States of the Union where one assessment serves as the basis of value, on which State as well as local taxes are imposed.

The government publication, already referred to, "Wealth, Debt and Taxation," in its Table No. 20, gives for each County in the United States the estimated true value of real property and improvements and the assessed value of the same kinds of property.

From the figures furnished by the publication, I have prepared a table of the average which obtains for each State, and the highest and lowest ratio between estimated actual and assessed value for purpose of taxation, which obtains in the respective counties.

To read this table would prove wearisome to you as well as to me, and I therefore refrain, but I have annexed it to this paper.

Here, I will group the States into six classes. There are four

States in which the real property is assessed at from 15 to 23 per cent of its estimated true value; in those States, some of the counties range as low as 12, others as high as 40 per cent of estimated true value.

There are eight States where the averages for the States are from 30 to 40 per cent, and the counties in those States range from 17 to 90 per cent of estimated true value.

There are thirteen States where the averages for the States are from 41 to 50, and the counties in those States range from 26 to 87 per cent of estimated true value.

There are seven States where the averages for the States are from 52 to 60 per cent, and the counties in those States range from 20 to 80 per cent of estimated true value.

There are five States where the averages for the States are from 62 to 69 per cent, and the counties in those States range from 41 to 88 per cent of estimated true value.

There are seven States where the averages for the States are from 75 to 90 per cent, and the counties in those States range from 22 to 92 per cent of estimated true value.

One county in the entire United States — Suffolk County, Massachusetts — has assessed its real property at the same amount as its estimated true value, while New York City comes within 2 per cent of it.

I beg to repeat that, for the counties, the book gives only the estimated true and assessed values of real property; there is, however, every reason to believe that other kinds of property are assessed for purposes of taxation with like lack of equality and uniformity. What is the result? One county assesses its property at 20 per cent of true value, another at 80 per cent; both contribute to the revenue of the State on the basis of this unjust and unequal assessment, and it follows that one county pays four times as much to the State as the other.

And this condition is not peculiar to counties containing large cities, or counties in which lands are altogether or largely devoted to agriculture. The astute resident of the cities and the horny-handed farmer — all seem to be adepts at this sort of thing. Nor is the condition peculiar to any particular section. It exists in the fine old commonwealth of Pennsylvania, where the ratio in the counties ranges from 20 to 77 per cent; in

the great Empire State of New York, where the range is from 54 to 98 per cent; in Indiana, where the range is from 40 to 80 per cent; in proud old Virginia, where the range is from 22 to 80 per cent. In the State from which I have come — Louisiana — the range is 25 to 78 per cent. In far western California the range is 26 to 73 per cent. East, North, South, West — no section has a monopoly of the injustice and inequality which this condition betokens, though the people have, in the most solemn manner, again and again declared that taxation shall be equal and uniform. As we shall see farther on, in several of the States mentioned, this difference in ratio of assessed to real value in the counties has not the pernicious effect it has in other States.

For this difference in the ratio of assessed to real value in the counties of a State, one of the remedies suggested and tried is a board of equalization. This is a more or less expensive institution, composed of a certain number of men, who meet at certain stated periods, and endeavor, honestly I do not doubt, to equalize things.

What these boards have accomplished may be seen from the following:

Thirty-two States have such boards, among them are the States I have mentioned, except Virginia and Louisiana, though recently the latter has also instituted one; and, as we have seen, despite these boards, uniformity and equality are sadly lacking. So you have a board of equalization in your own State of Ohio, and yet the ratio of assessment to estimated true value of real property ranges from 27 to 70 per cent. They have a state board of equalization in Kansas, and the range is 17 to 42 per cent. But why go on with the dreary recital? It cannot and it will not be denied that there is no uniformity or equality in matters of taxation, under the prevailing system, where local and states taxes are derived from the same source.

A remedy for this does exist, a remedy simple and effective, and that is the separation of sources from which the state and local taxes are drawn. Let the State obtain all the revenue it needs from the sources it may select, and say to the counties and municipalities, all the rest of the property you may tax for your purposes, as you see proper.

The adoption of the principle does not carry with it the designation of the class of property or other sources of revenue which may be selected by the State. In one State it may be determined to raise all revenue from certain sources, in another State conditions may dictate the selection of others. Whatever sources the State may take, the principle is not affected, and this principle, I repeat, is, let the State obtain what revenues it may require from sources which it will select, and which it will relieve from all local taxation, and, having done this, let it say to the counties and municipalities, you may obtain what revenue you need from the sources of taxation which the State has not elected.

A discussion of what sources should be selected by the State is therefore not within the scope of this paper, nor involved in the principle here advocated. The legislature should be relied on to choose and, in the great majority of instances, would, I believe, choose wisely. If it were well advised, it would select only such sources as are not dependent on assessment made by the officers of the respective counties. It would select such sources as could properly be assessed by a state board. Lines of railway and equipment, telegraph and telephone lines, express companies, insurance companies, all furnish sources for revenue, which can easily be assessed by a board sitting at the state capital. Properties of the kind mentioned run usually through many counties; there is nothing local about them; and they furnish ideal subjects for taxation for state purposes, while real estate, live stock, merchandise and similar classes of property, including intangible property, are local in their character. A house, a farm, cattle, merchandise, are usually in one county, and should be the sources from which local taxes are drawn.

Adopt the principle here advocated, and you rid yourself of the need for more or less ineffective and expensive state boards of equalization; you rid yourself of what is, in reality, a competition between the counties in each State, to see which can escape with the least contribution to the income of the State, and you rid yourself of the inequality and lack of uniformity, due to the present system, of having the State and counties and municipalities all taking their income from the same source.

The proposed reform does not run counter to the most con-

servative view one may have on the subject of taxation. You may continue to attempt to tax all kinds of property equally, or you may tax one class of property at one rate and other classes at other rates. You may exempt, or not, as you will; not a single right of any one is violated, except the right to make the people in one county pay more than their share of state taxes, while others pay less.

Wherever the subject has been examined, the separation of sources has been adopted. It has been adopted partially or altogether in the States of Pennsylvania, Connecticut, New Jersey, New York, Wisconsin and Oregon, and it is very seriously discussed in some eight or ten other States.

The commission appointed in California to examine the subject has reported in its favor. The commission appointed by Governor Folk of Missouri reported in its favor. Governor Folk indorsed the recommendation, and the legislature of the State has adopted several acts which submit to the people certain changes in the constitution of the State necessary to put the method into practice.

That the proposed method will effectually eradicate the existing inequality between the amount of taxes paid by the different counties to the State cannot be denied, for the property in the county, *i.e.* the houses, farms, cattle, merchandise, etc., will not contribute to state taxation at all. If the property in a county is assessed for county purposes alone, if the assessment does not serve as a basis for any state tax, it cannot and does not matter to another county whether the assessment is 10 or 100 per cent of true value. The county needs a certain sum for its budget; if it assesses the property at a low valuation, the rate of taxation will be higher, — that will be the only effect of varying valuations.

But I believe that the complete eradication of the unequal contribution by different counties to the revenue of the State will not be the only effect, though this in itself would justify the change. I believe the adoption of the system will tend to equalize and make uniform the amount of taxes which the various kinds of property pay in each county, and I believe it will enable each county intelligently to consider the incidence of taxation.

The different counties in a State have varying needs. A county with a large city in it may find it advantageous to have a certain method of obtaining revenue. Another county, devoted largely or altogether to agriculture, might prefer another method.

Where all tax legislation is had in the legislature of the State, these varying needs have no opportunity to assert themselves effectively. Very frequently the interests of the cities apparently clash with those of the country; what suits one does not suit the other; the majority controls, and the minority suffers from the imposition of a method not suited to its needs.

As long as the present system obtains, this cannot be avoided. The legislature cannot adopt one method for one county or class of counties, and another method for another county or class of counties. The legislature must of necessity adopt some method which, while quite satisfactory to one or more, is rarely so to all counties. If, however, we separate the sources from which the State draws its support, and leave to the counties and municipalities the management and control of their own methods of taxation, we substitute for the rigid system, prescribed by the State, and to which the county must adjust itself, a flexible system which will adjust itself to the needs of the county. You establish a species of home rule in this most important branch of government activity, and we may be quite certain that each community will sooner or later find the method best suited to its needs; and, when it does that, it may not obtain a method by which all kinds of property will be taxed with perfect equality and uniformity, but it will come much nearer to it than we do now, and each locality will in addition be able to so direct the incidence of taxation as to promote the purposes it desires to promote, and to hinder the activities it desires to hinder. Adopt this method, and every year, when the proper authorities meet to impose taxes, the taxpayers will attend in person because the seat of government is at home, ideas will be advanced and debated, and the freedom of debate will result in progress and improvement in method and system.

All this can be accomplished by having the constitution of a State declare that the legislature shall, at its session, determine

the sources from whence the State shall draw its revenues, and the amount which shall be obtained from these sources; that the counties and municipalities within them shall derive their revenues from sources not selected by the State.

To give the largest measure of home rule, the constitution should not contain any declaration tending to exempt certain classes of property, it should not contain any declaration limiting the tax rate, and it should not declare that all classes of property shall be taxed equally. The constitution should grant the greatest liberty on the subject to the counties, and we may be quite sure, that, at least in the great majority of cases, the freedom will not be abused.

The love of righteousness, the progress and prosperity that will certainly follow enlightened and intelligent methods of taxation, made possible by the freedom of each community to manage its affairs, all will serve to prevent its abuse.

Let me say, in conclusion, the adoption of this method will not produce perfect equality and uniformity between the different kinds of property and different owners of the same kinds of property. Human fallibility and various pernicious influences will perhaps always prevent those ideal conditions, but the more intimate relation between the taxpayer and the taxing authorities, which will result from home rule in these matters, is certain to make for better conditions than those we have.

TABLE

1. In Alabama the average assessment of real estate for the State is about 45 per cent, the counties range from 37 to 60 per cent.
2. In Arizona the average is 34, the counties range from 17 to 50.
3. In Arkansas the average is 40, the counties range from 20 to 90.
4. In California the average is 50, the counties range from 26 to 73.
5. In Colorado the average is 40, the counties range from 21 to 67.
6. In Connecticut the average is 80, the counties range from 64 to 87.

7. In Delaware the average is 57, the three counties are respectively, 52, 55 and 68.
8. In California the average is 35, the counties range from 29 to 49.
9. In Georgia the average is 52, the counties range from 37 to 58.
10. In Idaho the average is 42, the counties range from 30 to 60.
11. In Illinois the average is 15, in the counties the average is about maintained.
12. In Indiana the average is 60, the counties range from 40 to 80.
13. In Iowa the average is 20, the counties range from 18 to 25.
14. In Kansas the average is 23, the counties range from 17 to 42.
15. In Kentucky the average is 62, the counties range from 41 to 76.
16. In Louisiana the average is 50, the counties range from 25 to 78.
17. In Maine the average is 75, the counties range from 66 to 80.
18. In Maryland the average is 65, the counties range from 46 to 70.
19. In Massachusetts the average is 90, the counties range from 75 to 100 in Suffolk.
20. In Michigan the average is 62, the counties range from 45 to 75.
21. In Minnesota the average is 38, the counties range from 22 to 55.
22. In Mississippi the average is 53, the counties range from 34 to 80.
23. In Missouri the average is 41, the counties range from 25 to 59.
24. In Montana the average is 44, the counties range from 21 to 50.
25. In Nebraska the average is 16, the counties range from 12 to 30.
26. In New Hampshire the average is 66, the counties range from 55 to 70.

27. In New York the average is 90, the counties range from 54 to 98 in New York City.
28. In North Carolina the average is 60, the counties range from 20 to 85.
29. In North Dakota the average is 30, the counties range from 20 to 35.
30. In Ohio the average is 46, the counties range from 27 to 70.
31. In Oregon the average is 30, the counties range from 20 to 40.
32. In Pennsylvania the average is 58, the counties range from 20 to 77.
33. In Rhode Island the average is 75, the counties show very little variation.
34. In South Carolina the average is 47, the counties range from 30 to 67.
35. In South Dakota the average is 46, the counties range from 36 to 67.
36. In Tennessee the average is 69, the counties range from 32 to 88.
37. In Texas the average is 49, the counties range from 23 to 74.
38. In Utah the average is 44, the counties range from 25 to 50.
39. In Vermont the average is 77, the counties range from 50 to 80.
40. In Virginia the average is 55, the counties range from 22 to 80.
41. In Washington the average is 46, the counties range from 22 to 50.
42. In West Virginia the average is 50, the counties range from 30 to 70.
43. In Wisconsin the average is 76, the counties range from 54 to 96.
44. In Wyoming the average is 32, the counties range from 29 to 50.

THE LIMITATIONS OF THE PURPOSES FOR WHICH TAXES MAY BE LEVIED

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THE question which I am to discuss at this hour may mean either: (1) What should be the limitations of the purpose for which taxes may be levied, that is, to what purposes should the levy of taxes be limited? or (2) How shall the limitations of the purposes for which taxes may be levied, be secured, that is, how shall the tax levy be effectively limited to proper purposes? The first of these questions involves the question of the proper objects of expenditure; the second question involves an examination of correct principles of procedure in the assessment and collection of taxes. The economist is likely to consider only the first of these questions; the lawyer and administrator, only the second. A complete treatment calls for a consideration of both.

The discussion of the first of these questions, what should be the limitations of the purposes for which taxes may be levied, must become in the main, therefore, and first of all, an inquiry into the nature of governmental functions. Whatever function the State in the last analysis assigns to its government is a legitimate function, and if, for the exercise of such function, the government must rely on revenue from taxation, then the performance of such function constitutes a public purpose for which taxes may be levied. The determination of the purposes for which taxes may be levied, not less than the power to tax, is a characteristic, a quality, of sovereignty. There are no inherent limitations upon the purposes for which taxes may be levied which can be imposed upon a sovereign state from without. But the State, in determining upon its functions, in formulating its social choices and its social will, is amenable to

reason more or less consciously exercised and guided by observation and experience and reflected notably by the more thoughtful and critical of its members. It is precisely at this point that a gathering like the present may be hoped to have its share in the formation of the public opinion, which, by and by and from time to time, will express itself authoritatively through its representative legislatures or ultimately in the courts — I say, perchance, ultimately in the courts, for in the last analysis the courts as well as the legislative assemblies gather up and express the public or social judgment and decree. Yet the courts are not in the foreground of the problems of taxation. It is with the legislature that the presumption of our law rests the power of the State in determining the public purposes for which taxes may be levied. It is our legislative assemblies, state and local, which in our system are the dynamic agencies of social peace and social welfare, and it is accordingly upon these, that is, upon the men who make up their membership, that the serious study of taxation must be urged.

First, then, let us undertake to state the *theoretical limitations* of the purposes for which taxes may be levied, or the proper objects of expenditure.

Although the classifications of the proper objects of public expenditure have been variously made by the different writers from Adam Smith to our own day, it is easy to discern a substantial agreement and harmony in the several analyses advanced. J. S. Mill, for example, classifies state functions as necessary and optional; Roscher, as necessary, ornamental, and useful; H. C. Adams, as protective, commercial, and developmental. An acquaintance with the items of expenditure which these writers place under these several classes shows practical unanimity with respect to the first class, which may be broadly described as the protective or regulative functions of government, and very considerable divergence in the other classes. In fact, there is much to say in favor of throwing the other classes together into one, which might be described as the questionable or debatable functions of government — questionable or debatable in the sense that each non-protective function must make its own defense, make showing of its own social expediency, before the government can legitimately enter

upon it. Some degree of unanimity is reached, even with regard to the second class, if we group the non-protective functions broadly as embraced under the concept of public works. Debate respecting the limitations upon this class of public purposes would then shift to largeness of latitude to be accorded to the scope of public works.

If we search for a positive or *historic order of development* as a scientific basis for the enumeration or classification of state functions and seek to reconstruct the concrete order of their development, we come to classifications substantially similar to those above cited from various economists. Our result might be tabulated thus:

1. Defense: External war; internal peace.
2. Justice: Establishment of courts (judges) and judicial procedure.
3. Public works: community of social effort, taking form in industrial and cultural enterprises.

It is perhaps too much to claim that the above represents a rigidly exact order of development; it is enough to say that this, in rough outline, represents the concrete order of development. These several functions have indeed, in a way, developed side by side, but with a changing emphasis in successive epochs of social evolution. We may indeed concede that, in their elementary forms, they seem to have developed spontaneously, but we know they have grown at varying rates. Furthermore, certain functions which would now be classed as public works were originally subordinate parts of defense or justice. For example, the public post developed as an incident in the better conduct of war. Every careful student of political science must be impressed with the permanence and universality of these three classes of public purposes for which taxes may be or may have been levied in every civilized State. Some positive ground is gained by insisting on limitations to these purposes. This done, the question of interpretation would remain, and must needs continue, for no abstract statement of principles can free us from the problem of making practical application of principles.

It is in the third class that debate respecting limitations is still vital and opportune. Debate, we urge, respecting this

class is even demanded, lest the present growing tendency for the State to assign new functions to government shall break down government through an excessive imposition of new burdens on shoulders not now too strong.

The present tendency, every one knows, is to give this third class a larger and larger place in public budgets. This class has, in fact, become so large, particularly in view of the new developments of functions within the class, that it has led Professor Adams, for example, to seek for a readjustment of proportions by throwing together the first two historic classes, namely defense and justice, into one, and calling it protective, while he subdivides the remaining public works class into two distinct classes, namely the distinctively commercial or industrial, and the distinctively cultural or developmental.

The careful study of public works as a public purpose necessitates new and present attention to the wise *differentiation between duties to be assigned to central and local governments*. Attention must incessantly be urged that neither the State nor any of its subdivisions, such as the municipality, can engage in industry without justifying every specific enterprise by unquestioned evidence of its public expediency; and even then it remains to be shown that such an enterprise can have any claim, except in temporary and provisional manner, upon taxation as a source of revenue.

It is of the utmost importance on grounds of public expediency, and this includes grounds of public morality, that a distinction be drawn between those public works, such as highways, which may be recognized as proper public purposes for which taxes may be levied; and public works, such as municipal public service like light and transport facilities, which, on account of their essentially industrial character, must be made to pay for themselves, or in the failure of municipal or public management must be let to private operation or operation by contract under public control. History is full of imperative lessons on this subject, and the last chapter of experience in this field has not yet been written.

Suppose we rest the problem of determining what constitutes a public purpose on grounds of public expediency instead of *a priori* analysis, our problem is still a vast one, for it involves

the exact balancing against one another of public and private needs; it involves the making of provision for public and private needs in the ratio of their economic importance. In our search for a delimitation of the proper objects of public expenditure we are compelled the more to rely on an analysis of social needs, with incidental recognition of the value of an examination of the historical order in the development of state functions, because absolutely reliable statistical lines of approach to the solution of our problem lie hopelessly removed from present available use. In the present conditions of the science of finance, as Adams observes, "the sociologic significance of government presents a problem that has never received adequate treatment from economists and financiers,"¹ and it is necessary to resolve this problem first before an intelligent system of keeping public accounts can be developed, for without it we shall be without standard or norm by which to judge in a comparison of accounts.

In the determination of a public purpose by analysis there is always one rule on which it is fair to insist; namely, that the tax levied for the given public purpose must in turn yield higher social dividends than the same amount left in the possession of the taxpayers; this is a rule given by deductive economics. And by the side of this is the equally important rule before adverted to, contributed by our system of law; namely, that the public purpose for which the tax is levied must pertain to the district taxed. If it cannot stand this test, it is not a public purpose within the meaning of the law or the economic analysis. These two rules will furnish tests by which many so-called public purposes can be read out of the list of proper objects for public expenditure.

Perhaps a further defense or explanation should be made for designating all non-protective functions as welfare functions which in their exercise involve the express creation of or indirect fostering of public works. The term "public works" is taken in the broad sense, which makes it coextensive with public service; and in this broad sense it is understood to include an educational institution as well as a courthouse or legislative hall, a postal route as well as a post office, a city park as well

¹ Adams, "Science of Finance," p. 36.

as a sewer system. By recognizing public works as commercial and developmental, as Adams does,¹ attention is drawn to the purely commercial which relate to industry directly and which may be described as direct aids to industry, such as highways and river and harbor improvements, and indirect aids to industry, such as bounties, subsidies and the debatable protective customs tariffs; while the developmental embrace expenditures for education, recreation and public investigation.

The student who turns to the law for clear authoritative limitations of the purposes for which taxes may be levied will soon find on careful investigation that *legal limitations* by law aim to define the taxing power rather than the public purposes for which taxes may be levied. Our ordinary legal limitations may be briefly stated: It is a general rule of our American law (1) that taxes can be levied for public purposes only; (2) that the legislature can determine ordinarily what shall constitute a public purpose, that is to say, the presumption of the law is in favor of the legislature; (3) that the act of the legislature establishing a tax may be reviewed and declared void by the courts if not found to be for a public purpose. In the specific application or interpretation of these rules, practice varies.²

Constitutional limitations on taxation usually consist in limitations on the taxing power accorded to the legislature, and statutory limitations define the taxing power of subordinate divisions of the State rather than the limitations of the purposes for which taxes may be levied. Some restrictions of the latter character do, however, occur; and such limitations come for the most part under the general rule above cited that the levy of taxes by a commonwealth or by local subdivisions of the government must be for public purposes within the district upon which the tax falls.³ This paper does not discuss the limitations upon the power of taxation. Some of these limitations are inherent; the State, for example, cannot tax property where there is none, nor can it tax property outside of its territorial limits; neither can government delegate its powers of taxation, nor can it tax itself or its agents or agencies.

¹ For Adams's analysis see his "Science of Finance," §§ 11-14.

² See Goodnow, "Cases in Taxation," and Cooley on Taxation.

³ See Cooley on Taxation, Ch. V.

Such limitations should not be confused with the problem which deals with the determination of the limitations upon the purposes of taxation.¹

An examination into the proper limitations of the purposes for taxes cannot be adequate in our time without some notice of what Adolph Wagner has called the *socio-political purpose of taxation*. In the summary of the theoretical limitations of the purposes for which taxes may be levied, I gave no place to this note except as it may be found to have scope for an incidental influence in connection with what I called the cultural or developmental function of government. In Wagner's view of the matter there is an altogether different purpose in taxation than the securing of revenue for some concrete direct public purpose; it is, indeed, nothing less than an effort to use taxation as a lever for the equalization of the inequalities in fortune, the inequalities in the distribution of wealth.² Closely allied in its practical bearings to Wagner's socio-political theory of taxation is Henry C. Adams's brilliant section on "Taxes as a Means of Artificial Selection."³

Finally, we must mention the support of the government itself as a public purpose for which taxes may be levied. The clear recognition of this sort of public expenditure, as distinguished from grants to princes or to public officials, involved a process of slow and painful evolution. But we have at last reached clear views, though possibly not solid ground, on this question. Neither the will of a prince nor the desire of a public official constitutes a public purpose.

¹ For a good example of constitutional limitations of the power of taxation, see Federal Constitution, Art. I, Sec. 8, par. 1, and Sec. 9, pars. 4, 5.

² For a statement of Wagner's socio-political theory of taxation, and a brief criticism thereof by E. R. A. Seligman, see Bullock, "Selected Readings in Public Finance," pp. 178-184.

³ Adams' "Science of Finance," pp. 411-420.

METHODS OF ASSESSMENT AS APPLIED TO DIFFERENT CLASSES OF SUBJECTS

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I. INTRODUCTION

A. SIGNIFICANCE OF SUBJECT. — The fundamental thing in any system of taxation is the assessment. "Without a valid assessment no subsequent step can have any color of validity." An enduring system of taxation must be founded on justice and equity. This places on the assessor a double duty: he must find all taxable property, and he must assess it at a fair and just valuation. With the citizen it is the justice, rather than the size, of the burden of taxation that counts. As Judge Cooley well says, "The assessment is therefore the most important of all proceedings in taxation, and the provisions to insure its accomplishing its office are commonly very full and

particular." In the report of the New York Special Tax Commission, issued this year, it is stated that, "In many respects a board of assessors is the most important public body known to our government; if it fairly and honestly performs its duty, it will see that the burden of maintaining the government is fairly and honestly distributed upon those who should be willing to bear the burden, and who, under the law, are required to bear it." While it is evident, of course, that the government cannot give to the assessor courage and energy or otherwise improve his nature, it is also equally obvious that it can and should provide a system of assessment, simple, just, and workable under the prevailing limitations of human virtue.

B. AIM OF THIS PAPER.—Forty-eight States and Territories are now experimenting with methods of assessment, trying to find the ideal system. Success, more or less complete, has been reached by few, if any. This paper aims to give an account of all the principal methods of assessment now in force in the United States. It also aims to draw conclusions from the evidence thus presented, and make certain recommendations looking to the improvement of our assessment systems.

C. METHODS PURSUED.—To keep this discussion within reasonable limits, only the most important classes of subjects have been selected for treatment. These are discussed separately under their appropriate titles. Subjects peculiar to certain localities, and having, therefore, only local interest, are omitted. It is believed, however, that no essential principles of our present-day assessment are missed on this account. Only a few court decisions are cited, and these apply to general methods of assessment of national importance. While these decisions may seem like mere commonplaces to students of taxation, yet they will doubtless prove new and valuable to some of our state legislators.

This paper deals necessarily with the general property tax, since that is the tax in very general use throughout the country. No attempt is here made to set forth the evils of this tax, although I agree with those who consider it long since outgrown. Since its death is a very lingering one, if it be dying, we must deal with it as it now is. The progress made by the few States which to-day stand conspicuous for efficiency in

assessment will be reported in detail. And hence, as intimated above, no rhetoric will be wasted in describing the evils of the present system. A simple record of facts will be given, emphasizing the best, rather than the worst, features of the system as to-day administered.

Part II deals with Assessment of Certain Classes of Subjects.

Part III deals with General Methods of Assessing and Equalizing.

Part IV deals with the Assessor.

Part V deals with a Summary and Recommendations.

Part VI consists of tables exhibiting facts of assessment in the different States and Territories.

II. ASSESSMENT OF CERTAIN CLASSES OF SUBJECTS

A. REALTY. — A general uniformity in assessing realty prevails throughout the United States, with variations in the details. Assessors must assess it from actual view of the property, and at its actual cash value.

Frequency of. — Most States require it to be assessed annually or else once in two years. Other States (Illinois, Nebraska, Indiana, North Carolina, Vermont) have it assessed but once in four years. Mississippi now has four years, but will go on the two-year basis in 1909. Another State, Ohio, assesses realty but once every ten years. Of course, in these instances, where the assessments are so far apart, provision is made for adding improvements to the realty assessment when necessary and proper, and likewise for making subtractions when needed.

Land and Improvements Separately. — The old-fashioned method of assessment simply lumped land and buildings together in one sum and listed this as the value of the realty. The newer way is to list land and improvements separately (Indiana, Montana, North Dakota, Wisconsin, New York). Assessors are instructed to value buildings separately from the land, to estimate the value of the entire property including the buildings, and then "estimate" the value of the land without the buildings, the difference being the value of the buildings. Some assessors have already objected to this as requiring too much "imagination" on their part.

Vacant Lots. — A Connecticut report on taxation made

eleven years ago set forth the familiar doctrine that "Many owners of vacant lots, held for speculative purposes, contend that since these yield no income they should not be taxed proportionately to other near-by estates containing buildings and producing rentals." "This contention," the report continues, "is an erroneous one, for it is asserted by many of the most noted writers upon the subject of economics that *increasing value is income*." This phase of the single tax is coming into more and more favor with city assessors in many regions. Thus a city assessor of North Dakota in 1907 asked and secured from the State Board of Equalization an increase in the assessment of vacant lots, stating to the board that "this Henry George theory is all right taken with a few grains of salt."

St. Paul Method. — In 1896 a new system of assessing city realty went into operation in St. Paul. Values of corner lots and of lots next to corners were computed from the values of the center lots in each block. The center lots being first appraised by a committee of citizens, the values of corner lots were found by means of ingeniously constructed mathematical diagrams. The following table shows the ratios assumed to exist between the values of the corner and second lots, and of the middle lots, where the lots are twice as long as they are broad and the corner lot has its shorter frontage on a street where the frontage is worth twice as much per foot as on the side street, these middle lots also fronting on the better street.

RATIO OF POORER FRONTAGE TO BETTER	RATIO OF CORNER LOT TO MIDDLE LOT	RATIO OF SECOND LOT
.1	1.11	....
.2	1.14	1.02
.3	1.17	1.03
.4	1.22	1.03
.5	1.28	1.04
.6	1.36	1.05
.7	1.48	1.06
.8	1.60	1.08
.9	1.74	1.10
1.0	1.90	1.12

Buildings were assessed separately by eight special corps, eighty-two men doing the field work. Three sets of blanks were used covering (1) residences, (2) stores with halls above or living rooms, (3) large buildings. These blanks had spaces for fifty facts. A committee of architects adopted a plan for valuing ordinary buildings, by which they could be valued at so much per square foot of ground covered.

This plan has been followed with general satisfaction ever since. But there has been no thorough and complete revision of the assessment since 1896. It is now looked upon in St. Paul as the only scientific method of procedure.

History of Connecticut Methods. — Until 1819 Connecticut taxed real estate not according to its value, but in proportion to the annual income which, on the average, it was deemed likely to produce. Lands, as distinguished from buildings, were put on the list at a fixed rate for each kind, prescribed by statute. The best meadow land went into the list at \$2.50 an acre; plow land at \$1.67; pasture at \$1.34; wood lots at 34 cents each, etc., not because these sums were deemed to be the value of the lands, but because they were thought to represent the average income they would produce. Under such a system there was little opportunity for evading taxation. The acreage of each farm and the general character of each lot were readily ascertained, and the law then fixed the rate of assessment. When this scheme was abandoned, the method of assessing the property direct took its place. A board to equalize the assessments, in reality like our modern boards, was created. It made a record of accomplishing "substantially nothing," and was accordingly abolished. In 1867 an interesting act went into effect, requiring certain district commissioners to examine in each town a "sufficient number of homesteads" known as village property, and at least ten farms scattered over the town, and enough other taxable property to ascertain the average actual cash value thereof. A table comparing actual and assessed values was then to be prepared for the Comptroller. From this time on the study of the subject became more serious, and methods balanced between centralizing and decentralizing control of assessments. Out of the confusion has been evolved the present system centralized

in the State Board of Equalization and the Tax Commissioner.

B. PERSONAL PROPERTY, GENERAL. — Little need be said about general personal property, since it is to its differentiated forms that we must look for specialized methods of assessment. New York, of all the States, seems to have the weakest and most ineffectual way of assessing personal property. The law makes the broad requirement that the assessor shall "ascertain by diligent inquiry all property and the names of all persons taxable." There is no listing of separate articles. Hence personal assessments are "vague guesses," as is illustrated by the fact that several prominent multi-millionaires of New York City were assessed in 1907, on personalty, for less than the ordinary village merchant in most of our States (Report Special Tax Commission, New York, 1907, pp. 58-59). The method prevailing in most of the States is that of West Virginia, for instance; here it is the duty of the assessor or his assistants to see every person in his district who is liable to taxation, and obtain from him a sworn statement of his property, the personalty being listed under various sub-heads according to its class. Texas emphasizes the point of calling upon each person. "See every man in person" was one part of the instructions given to the 1907 assessors. Alabama has the more primitive fashion of requiring the taxpayer to call on the assessor. The assessor makes his headquarters for a few days in each precinct of the country, due notice of which has been given to the public. There the taxpayer must call and be assessed. He must first take oath that he is going to tell the truth, then, after being assessed, he must take a second oath that he has told the truth. At least the law requires this procedure. If taxpayer fails to appear, the assessor must reach him by mail or see him personally and obtain the proper list. North Carolina and other Southern States have a similar provision covering listing of property by taxpayer. Some States require the assessor to fill out the lists; others require the taxpayer. Oath taking is common, though not universal.

In spite of statute requirements, each assessor, when in the field at work, is largely a law unto himself. The question is, then, what methods does he, individually, adopt to find all

property and to value it at its full cash value? We get much light on this from replies sent in by local assessors of Connecticut (12 Bureau of Labor, Connecticut). Over three hundred assessors wrote answers to these two questions:

1. What means are used to ascertain if property should be listed higher or lower than last previous valuation?

2. What means are used to ascertain value of personal property?

The replies ran as follows: "Personal observation." "Sworn lists of owners." "Abstracts of previous years." "None." "Governed by recent sales in neighborhood." "Not attempted." "By attending to our business." "Common sense." "By lists of previous years." "None, except to nose around for a bicycle or a new horse. Houses are never entered nor lists of owners demanded." "Guess at it." "Guess work."

This is a true picture of the assessor at work, drawn by the assessor himself.

C. MERCHANDISE, STOCKS OF GOODS OF MERCHANTS AND MANUFACTURERS.—The Ohio law may be taken here as typical. The merchant or manufacturer lists the average amount of goods on hand for each month of the year, and from this is obtained the net average for the year. This net average gives the amount assessed for taxation.

As to the actual practice of the assessors, we may turn again to Connecticut, where over three hundred local assessors replied to the question, "How is value of stocks of merchandise ascertained?" The answers run as follows: "By asking," "As returned by the owners," "Sworn statement of owners," "By guess."

It is evident from these replies that assessment here is very largely a matter of self-assessment.

D. MORTGAGES, CREDITS, ETC.—This field of assessment shows a wide range of experimentation. Without going into an elaborate discussion of the taxation of intangible personalty, I will state briefly the general methods now obtaining for assessing this species of property. The majority of the States still leave this a matter of self-assessment. That is, the assessor provides a blank form for the taxpayer containing, among other headings, one for notes, bonds, mortgages, etc. The tax-

payer is supposed to list these intangible forms of property, exactly as his other property is listed. He may be called in for an oath or affirmation that he has listed all his property. Rarely, however, does the assessor go beyond this perfunctory and fruitless method. To help the assessor find this class of property Pennsylvania has worked out an efficient method. The register of deeds and mortgages shall keep a record of instruments filed securing the payment of money. Prothonotaries and clerks of courts shall keep a record of bills, bonds, judgments, or other instruments securing a debt, entered on record in their office. These records shall be placed in the county commissioners' offices or with the boards of review of taxes. And when the record shows that the owners of these credits live in a different county from that containing the record, this fact is communicated to the proper county. And when the assessment rolls pass through the hands of the reviewers, these credits are added.

Idaho represents the other extreme by simply exempting mortgages from taxation, her law providing specific exemption of "all dues and credits secured by mortgage or other lien." Alabama, New York and Virginia escape one difficulty of assessment by requiring a recording tax which is paid once for all when the mortgage is recorded. Indiana attempts to find the mortgage holder through the mortgagor. The mortgagor is exempt from taxation upon his real estate to the amount of \$700 only, but in no case can the exemption exceed half the assessment on his real estate. He must furnish the name and address of the mortgagee to the assessor. In this way mortgages are very generally discovered in Indiana, it is claimed.

The Wisconsin law for assessing mortgages marks a recent trend in legislation (Ch. 378, laws of 1905). This law provides that whenever "taxable real estate shall be subject to mortgage such mortgage for the purposes of taxation shall be deemed an interest in such real estate and shall be assessed and taxed as such interest in the assessment district in which such real estate is located, and not otherwise, and may be separately assessed and taxed as hereinafter provided. . . . At the option of the mortgagor both such interests may be assessed and taxed together, without separate valuation, to the mortgagor or occupant the

same as unincumbered real estate." The theory here is that each will be assessed on his proper share — the mortgagee on the mortgage as representing an equity in the land, and the mortgagor on the remaining value of the land. It does not work out this way. In Wisconsin in 1904 there were recorded 50,330 mortgages, and all of these but 31 contained the stipulation that the mortgagor should pay all taxes on the mortgaged premises.

The Wisconsin method holds in three other States. This is cited here to show that the assessment of mortgages is a problem as yet unsolved. With the various methods of taxation of mortgages this paper has nothing to do.

E. BANKS. — The assessment of incorporated banks has been greatly simplified and unified by Section 5219 of the Revised Statutes of the United States, providing for state taxation of shareholders in national banks.

"Nothing herein shall prevent all the shares in any association (national bank) from being included in the valuation of the personal property of the owner or holder of such shares, in assessing taxes imposed by authority of the State within which the association (national bank) is located; but the legislature of each State may determine and direct the manner and place of taxing all the shares of national banking associations located within the State, subject only to the two restrictions, that the taxation shall not be at a greater rate than is assessed upon other moneyed capital in the hands of individual citizens of such State, and that the shares of any national banking association owned by non-residents of any State shall be taxed in the city or town where the bank is located, and not elsewhere. Nothing herein shall be construed to exempt the real property of associations from either state, county or municipal taxes, to the same extent, according to its value, as other real property is taxed."

The majority of States now follow this rule. The assessor determines the value, from the bank's own statement, of the shares of stock, and these are then assessed to the several stockholders, the bank paying the tax and collecting it back in turn from the shareholders. Real estate, being separately assessed, is subtracted from the bank's capital. Surplus and undivided profits are usually added to the capital stock. There

are minor variations from this method of assessing banks. New Jersey provides that the bank shall furnish a list of the stockholders, and that each stockholder is then assessed and taxed at his home, not at the bank.

Florida seems to have the most radical feature in the matter of assessing deposits to the bank (Ch. 5596, No. 1, Sec. 9, Act approved June 18, 1907). The new law there provides that the bank shall make a return for assessment at the real value of all such deposits, and shall be liable for the tax on the same. The law also provides for assessing the individual depositor on his credits, including deposits, thus making a clear case of double assessment.

F. CORPORATIONS, GENERAL. — Professor Seligman several years ago named thirteen distinct ways of taxing corporations. The Report of the Massachusetts Committee on Corporation Laws, 1903, discussing all corporations except municipal, banking and public service, enumerates the following methods of corporation taxation:

1. General Property Tax on Corporations.

A. Tax on Real Estate; common in all the States.

B. Tax on Separate Items of Corporate Personal Property.

(1) Tax levied on tangible and intangible personalty.

(2) Tangible personalty only assessed, the intangible being reached through tax on capital stock.

(3) Valuing plant or enterprise as a whole on basis of money invested, deducting realty and taxing remainder in a lump sum as the capital of the corporation.

(4) Tax on capital stock or shares, from assessment on all tangible and intangible personalty.

C. Tax on Capital Stock.

(1) Tax on corporate excess. This "excess" is sometimes known as good will, franchise, etc.

(2) Tax on total capital stock. The taxable value of this capital stock is variously ascertained. The following are common methods: market value; "actual value" (in case there is no market value); market value considered in connection with gross earnings, with net earnings, dividends,

and surplus, with the bonds, rate of dividends and amount of surplus; value of the use of the property; cost of duplication with other evidence.

D. Tax on Bonds. "If the corporation has a bonded debt, the corporate property is security for the outstanding bonds, and the share value represents only the equity in the property subject to the lien of the bonded debt. The corporate bonds, therefore, represent a portion, and often the most considerable portion, of the corporate assets, and manifestly should be made liable to taxation, either by taxing the individual bondholders, or by taxing the corporation on the value of its bonds in addition to its shares of capital stock. Some States, however, instead of so doing, deduct the amount of the bonded indebtedness from the share value. This is done on the analogy of deducting debts from credits, but the conditions are wholly dissimilar, and such deductions cannot be justified even if the bonds are taxed to the individual bondholders. The judicial ruling in Minnesota that such deduction destroys the whole principle of uniformity of taxation, and is, therefore, unconstitutional, seems entirely sound." (*State vs. Duluth Gas and W. Co.*, 76 Minn. 96.)

- (1) Stocks and bonds combined. (The legality of this is discussed below.)
- (2) Tax on bonds held by residents, said tax being paid by the corporation.

2. License Taxes on Corporations.

A. Charter Fee.

- (1) Fixed sum regardless of size of capital stock.
- (2) Fixed percentage of authorized capital stock.
- (3) Sum graduated according to amount of authorized capital stock.

B. Annual Franchise Tax.

- (1) Fixed sum.
- (2) Graduated sum.
- (3) Fixed percentage of par value of capital stock.

- (4) Percentage of capital stock employed in State, graduated according to dividends on par value of capital stock.

C. Occupation Tax.

- (1) On manufacturing corporations.
- (2) On mercantile corporations.

Taxing Stock and Bonds, Legality of. — There is little doubt about the wisdom and efficiency of taxing a corporation directly for the amount of its stocks and bonds, allowing it to collect back this amount from dividends and interest. But there are certain legal difficulties. Resident shareholders and bondholders can of course be taxed at the pleasure of the State. Non-resident shareholders can be taxed and the courts will uphold the constitutionality of the tax (*Tappan vs. Merchants' National Bank*, 19 Wall. (U.S.) 490; *Delaware Ry. Tax Case*, 18 Wall. 208; *New Orleans vs. Houston*, 119 U.S. 265; *State vs. Travelers Ins. Co.*, 70 Conn. 590; *First National Bank, Mendota vs. Smith*, 65 Ill. 44; *Tax Collector vs. Insurance Co.*, 42 La. Annual 1172). The difficulty comes in taxing non-resident bondholders. Such a tax has been held invalid by the United States Supreme Court (*State Tax on Foreign-held Bonds*, 15 Wall. (U.S.) 300). But in another case (*Savings Society vs. Multnomah County*, 169 U.S. 421) the Supreme Court held that a tax levied within the State upon a foreign-held mortgage which is secured by real estate situated within the State is constitutional. So we find States taxing mortgages held by non-residents. If bonds can be put in the same class with mortgages, where they do belong, there will no longer be any question as to their taxation. There is an irrepressible conflict between the legal viewpoint and the economic viewpoint. The Report of the New York Special Tax Commission of 1907 puts the economic situation clearly, in these words, after asking the question, "Should corporations be assessed on capital stock alone — the present New York method?" "From the economic point of view," continues the report, "bonds are not a debt but a part of the productive capital. Two corporations with an investment of a million dollars each, the one with an entire million in capital stock and the other with half a million in bonds, ought for the purposes of taxation

to be treated alike; yet at present we tax the one corporation just twice as much as the other. In our sister States, like Pennsylvania and Connecticut, this inequality has been redressed; but we still pursue the old plan, which we adopted from Pennsylvania and which has long since been abandoned there."

Pennsylvania Method. — The general principles followed by Pennsylvania in assessing her highly differentiated corporations can be briefly stated. To quote from her "Compendium and Brief History of Taxation" (1906):

"The Constitution and Acts of Assembly require that taxes shall be uniform upon the same class of subjects. It would be almost impossible to apply the same rules or method of arriving at actual values of the capital stock of a railroad company to that of an electric light company, water, land, natural gas, mining, brewing, trust, or insurance company. In view of the impossibility of adopting a uniform or single method of arriving at a valuation and assessment of all corporations, many years' experience in the assessment and collection of the State's revenues has resulted in the adoption of what might be called a sub-classification of the different subjects, the desire being to secure uniformity of valuation and assessment upon the same class of corporation taxables. A different form of blank is prepared for each class, calling for certain information, under oath, for facts and conditions differ in each class of corporations."

The courts have upheld this system, applying the rule to so much of the stock as is represented by assets actually employed in Pennsylvania. Concerning bonds, the courts have held that the tax on bonds of corporations is not in any sense or in any degree a tax on the corporation or its property, but on the individual citizen of the State who holds the bonds. The corporation merely collects and pays over to the State this tax from the resident bondholders (*Com. vs. Lehigh Valley R.R. Co.*, 186 Pa. 235; *Com. vs. Wilkes-Barre and Scranton Ry.*, 162 Pa. 614).

"Tap the Source." — A tendency, clearly illustrated in Pennsylvania's history, is spreading, namely, to abandon taxes on the security holder, and tap the sources of revenue instead. States first began to give up the effort to tax the holders of railroad securities and sought to tax the corporations directly

to the full extent of their taxable capacity. The laws of California and Arizona have gone so far as to explicitly forbid the taxation of both corporation and security holder, the Arizona law asserting that "shares of stock in a corporation possess no intrinsic value over and above the actual value of the property of the corporation for which they stand." This is the rule also in North Carolina, West Virginia, Ohio, Kentucky, and Wisconsin. Iowa and Missouri try to tax both.

Maine. — In Maine we find an extreme case of centralized assessment of corporations. Here the Board of State Assessors, annually, from sworn returns, assesses the corporations of the State. The list of corporations thus assessed comprises savings banks, railroads, telegraph and telephone, express, trust and banking companies, building and loan associations, palace car companies and several thousand general corporations. In this way the corporation is dealt with as an economic unit, rather than as a conglomeration of realty, personalty, machinery, franchise, etc.

Alabama and North Dakota. — Alabama and North Dakota present a unique method of assessing general corporations. From the total value of the concern the local assessor is to deduct the value of its real and personal property. The residue, if any, represents the value of the shares. North Dakota further provides that "indebtedness" shall also be subtracted, and the remainder, "if any," shall be listed as bonds or stocks. Reliance is here placed on finding and assessing the widely scattered security holders, a rather antiquated method.

G. INSURANCE COMPANIES. — Methods of assessing insurance companies vary with respect to such conditions as the company being foreign or domestic, being fire or life, being joint-stock or mutual.

The North Dakota law may be taken as typical for foreign insurance companies. This law provides that every such insurance company "shall at the time of making the annual statement of business done, as required by law, pay to the commissioner of insurance 2½ per cent of the gross amount of premiums received in this State during the preceding year. Upon payment of such sum the commissioner of insurance shall issue the annual certificate provided by law" (Sec. 4475, Code 1905).

This is merely a case of self-assessment and income tax.

Illinois bases the tax on net receipts. But the principle of assessment is the same.

New Jersey has a different basis entirely for assessing life insurance companies (Ch. 218, Laws of 1906). Life insurance companies shall be assessed and taxed upon the full value of their property, exclusive of real estate in the State and securities to the value of \$500,000. A further deduction is also made of the amount of their debts and liabilities (policies). The companies file statements with local assessor where principal office of company is located.

Some States use the Virginia method — leave assessment of all tangible property to local assessors, the State supplementing this with special forms of taxes. This is a question of taxation, however, rather than assessment.

H. TRANSPORTATION AND TRANSMISSION COMPANIES, GENERAL. — Concerning the assessment of these industries the two important questions to ask are: (1) Are they assessed by some central board? (2) Are they assessed as units? Some States now answer both these questions in the affirmative. Many answer but one in the affirmative. Two States (Rhode Island and Oregon) answer them both in the negative. That there is an encouraging growth in this matter we can readily see by noting the following legislative and constitutional changes made within the last half dozen years.

In 1900 North Dakota and Michigan amended their constitutions to secure improved control of these companies, Michigan abolishing her constitutional provision concerning railroads to cover telegraph, telephone, express, and car companies.

In 1901 Colorado, Indiana and Missouri extended the jurisdiction of the state board.

In 1902 Colorado, Iowa, Minnesota, Mississippi, Rhode Island and Virginia centralized in one way or another this form of assessment.

In 1903 Wisconsin dropped the gross earnings tax on railroads and placed these under a state board for assessment. Nebraska centralized the assessment of railways in a state board of equalization. Wyoming did likewise for her express companies. Oregon in 1906, under the initiative and referen-

dum, brought her express, telegraph, telephone, and car companies under the annual license system. In 1907 she almost succeeded in placing railroad assessments in the hands of a state board.

The tendency shown by the foregoing cases is clearly in the right direction. Some particular methods must now be examined.

I. RAILROADS. — In the methods of assessment in use in the individual States, the reader is referred to Part VI, Table II, and also the excellent report, "Compendium and History of Taxation in Pennsylvania," 1906, pp. 103-138. Only typical methods illustrating different principles of assessment can be discussed here.

Of the three general methods of taxing railroads, the Property Tax principle, the Income Tax principle, and the Fee principle, the first, or property tax system, is that most universally employed. In 1901 thirty-four States used the *ad valorem* tax, three supplementing it with a gross earnings tax. In 1907 forty-two States made use of the *ad valorem* tax.

The two principles involved in making the *ad valorem* assessment of railroads are these: First, Is the property assessed centrally or locally? And second, Is the property assessed as a unit or as a composite?

As to the first question, all States now, save Rhode Island and Oregon, have some form of central assessment. This duty falls to a state board, as a very general rule, although Ohio still uses local boards composed of the auditors of the various counties containing the railroad property. This phase of assessment may be considered as settled in favor of the central board. The discussion of the future will be on the advisability of having one central federal assessment of railroads, rather than forty-eight state assessments.

Units or Composites. — The second question, that of treating the roads as units, is farther from solution. Wyoming, North Dakota, and several other States still use the "composite" method. To make the matter concrete, take the constitution of North Dakota (Amendment 4). This requires the State Board of Equalization (an *ex officio* board consisting of the Governor, Auditor, Treasurer, Attorney General, and Com-

missioner of Agriculture and Labor) to assess the "franchise, roadway, roadbed, rails, and rolling stock of all railroads." The basis of this assessment is necessarily reports made by the roads themselves. Now, visit a state board of equalization in session and see what happens. Their task of listening to the long line of aggrieved representatives of the various municipalities and counties of the State, and of trying to equalize their claims, is a huge one. But their familiarity with conditions in the State enables them to do this with a rough approximation of justice, at least. But they lack both time and expert information to deal justly with the railroads. These roads have their representatives present to furnish the only "expert information" concerning the roadway and its value; the roadbed with its details of construction of so many yards of earth, gravel, stone, cinders, etc.; the rails, their length, weight, age, etc.; and the rolling stock, from the largest locomotives down to the smallest hand cars and push cars. With this mass of bristling facts before them, the board proceeds to value the road, on its physical basis alone, ignoring entirely the intangible item of *franchise*. This I believe to be a true picture of our ordinary state board of equalization at work to-day. The factor omitted, namely, franchise, vitiates the whole assessment. Yet this is the common method in rather general use throughout the United States.

Nevada. — Some States, however, must be singled out as having passed this period of adolescence in assessing railroads. Nevada is one of them. The State Board of Assessors in this State is composed of the county assessors, fourteen in number, meeting at the Capitol, with the Governor as chairman. In fixing the values of railroads, the statute requires that the railroad property shall not be treated as so much "land covered by right of way" nor "as so much iron," but as a complete operated line of road. The State Supreme Court (23 Nev. 283; 23 Nev. 432) has held that "the value of a railroad must be determined mainly by its net earnings, capitalized at current rates of interest, taking into consideration any prospective increase or decrease in the earning capacity of the road." This, of course, comes close to the rule of Henry C. Adams, to be mentioned later.

Michigan and Wisconsin Assessment.—Two States have made a valuation of the physical property of their railroads, and have done it with so much expense and such thorough accuracy as to give it an importance of first magnitude. Michigan did this work in 1900–1901; Wisconsin, in 1903–1904. Both of these States had been the home of the gross earnings tax, Wisconsin for 50 years; and both had found that while the roads were paying from 2 per cent to 5 per cent of their gross earnings, the farmers were paying from 7 per cent to 10 per cent of theirs. Hence they adopted the property tax for railroads.

In Michigan the Board of State Tax Commissioners employed Professor Mortimer E. Cooley, Professor of Mechanical Engineering in the University of Michigan, to make the appraisal of railway property. With the assistance of a large body of trained specialists he ascertained the cost of reproducing the property, *de novo*, and estimated its present worth. "The work attracted the attention of engineers and economists all over the country. It was the first work of the kind in the United States attempted on so large a scale."

The Wisconsin appraisal was very much similar, being conducted by Professor W. D. Taylor, of the Wisconsin State University. He, too, ascertained the two points, (1) cost of reproduction, and (2) present value of the physical properties. Some thirty-five men in all were employed, though not so many at any one time. The work was done with scientific thoroughness and completeness. The railroads cheerfully coöperated, handing in appraisals of their own in advance, as requested. In this way one set of figures was used to check up the accuracy of the other. To illustrate the expense of this for the roads it may be said that one road, the Chicago and Northwestern, had more than seventy men engaged in this work at one time and expended more than \$19,000 on it.

The Wisconsin and Michigan appraisals were in substantial agreement, the Wisconsin valuation being about \$5000 per mile above that of Michigan.

	REPRODUCTION COST	PRESENT VALUE
Wisconsin	\$30,900 per mile	\$25,000
Michigan	\$26,100 " "	\$21,500

For getting the value of the roads as a unit, including their franchise value, Professor Henry C. Adams, statistician of the United States Interstate Commerce Commission, was employed. He laid down the rule "that in the long run the true cash value of such property must be the capitalization of an assured income." His estimate of the actual value was reached by taking the average earnings for ten years, setting aside from this amount 5 per cent on the appraisal of the physical property, and capitalizing the balance on a basis of 7 per cent.

In the case of the Wisconsin Board, no hard and fast rules were followed. They increased the valuation of the physical property returned by Professor Taylor by 29 per cent and called it the assessed value of the railroads. This Tax Commission has practically unlimited powers in determining what factors shall be considered in making their annual assessments of railroads. The law is sound economically and legally. Suit was immediately brought against the State, when the first assessment was made in 1904, on the ground that the law was in conflict with the state and federal constitutions. This was a question of the utmost importance, not only to Wisconsin, but to every State in the Union applying the property tax to railroads. The court upheld the law in every particular. The decision of the court was in part as follows (Chicago & N. W. Ry. Co. *vs.* State, 128 Wis. 553, 108 N. W. 557):

"They (the state board) knew the law and their duty. They had a wide discretion in respect to the mere elements to be considered in making the valuation. If they thought the so-called valuation of physical property would aid them, they were permitted to procure evidence of that sort. We find, however, no satisfactory indication that they arrived at the value of the railroad property by adding together a valuation of visible things and one of other elements, or that they did anything else other than just what they were required to do by the statute, determined the value of the railway property in this State; that included the visible things and the franchise, not as separate things any more than the horse's blood, frame, internal machinery and other elements are separate things. All taken together constitute the horse; remove any one of the things essential to life and action, and all conception of the animate thing, the horse, disappears. To our minds the only reasonable inference is that the board, from all the evidence before it,

performed the duty that it was required to perform. The evidence as we read it is to this effect. The board considered the report of the person who, as before suggested, performed the feat of separating and valuing the physical property, the market price as to each company of its bonds and stocks for a period of five years, reports of the engineers of the railway companies as to the physical property, the gross and net earnings of each company, both in the whole and in this State, and other elements, and fixed the value of the entire property of each company in this State at its due proportion of the value of the entire system, not giving to any particular factor of the evidence any particular weight separate from the other, nor placing any particular value upon any particular element of the property separate from the rest. We see no infirmity in that in any respect. The board did not attempt to value the visible things at one sum and the franchise or any other intangible elements, separately or in combination, at another. The evidence given by the president of the commission is unmistakable as to what was done.

"He said: 'The board never made any estimate of the physical property of the road.' 'The board did not have any other evidence of the value of the property physically considered, than the reports of Professor Taylor and the railroad engineers.' 'The board considered the entire property of the railway company, including its franchises and other property, to be of the value stated, being influenced in that consideration by all the matters that related to that subject of valuation.' 'Those matters of stock and bond prices, the gross earnings, franchises and the net earnings were under consideration.'—'These data, price of stocks and bonds, gross and net earnings, were considered as evidence of the value of the company's franchise, to help the board in arriving at the value.' *'The property was valued as an entirety.'*"

"In working out the supremely complex problem of how best to tax railway property, under the constitutional rule of uniformity, a problem which has vexed legislatures and courts throughout the country for fifty years or more, as we before indicated, the legislature has a wide discretion. The necessity for treating railroad property differently from general property as to mere method of attaining the constitutional object is manifest. That necessity implies more than mere permission; it implies a constitutional command. All reasonable effort to respond to that command, instead of violating the constitutional rule, promotes the very equality it was designed to secure."

Professor Henry C. Adams and the United States Census Valuation.—In Bulletin 21 of the Bureau of the Census there appears

the "Commercial valuation of railway operating property in the United States: 1904." In this we have the expert method of Professor Adams. The aim is to secure the true cash or market value of the roads, having reference to the fundamental considerations; namely, the expectation of income from the use of the property, and the strategic significance of the property. The method, if brief, was to capitalize *true operating income*. The rate of the capitalization was obtained by an extended series of computation, which cannot be discussed here. See Bulletin just cited, or Report of Board of Commissioners of Assessment and Taxation, Oregon, 1906, pp. 191-196. In substance the rule is, divide net corporate income by the aggregate value of corporate securities.

Mileage Basis. — In assessing the rolling stock and other personalty of interstate railroads, most States now follow the rule of assigning to the State such a part of the total value of the property as the mileage of road within the State is of the total mileage of said road. This practice has been upheld by the Supreme Court (154 U.S. 421 and 163 U.S. 1). Iowa seems to make business rather than property the basis of the mileage apportionment. Her rule is, "If a part of any railway is without this State, then, in estimating the value of its rolling stock and movable property, they shall take into consideration the proportion which the business of that part of the railway lying within the State bears to the business of the railway without the State."

Question of Terminals. — Two distinct policies exist in regard to the assessment of railway terminals. Missouri is a type of the correct policy. The assessment is apportioned to the general mileage of the State. St. Louis gets no benefit from valuable terminals there. They have the same mileage valuation as the railway in the rural counties of the State. Virginia is typical of the wrong policy. In apportioning interstate earnings to this State, for example, using the mileage basis, her rule is, "from the sum so ascertained there may be deducted a reasonable sum because of any excess value of the terminal facilities or other similar advantages situated in other States, over similar facilities or advantages situated in this State." This view is wrong because it fails to treat the road as a unit.

The property was not valued as an entirety, as the Wisconsin court declared should be done.

J. CAR COMPANIES. — Little need be said about assessing car companies of the various kinds. Most of the States applying the property tax to this species of movable personalty have adopted the correct policy of valuing the company as a unit, by a state board, and then apportioning to the State a certain share based on mileage. The legality of this method has been repeatedly upheld by the United States Courts (*e.g.* see *Pullman Car Co. vs. Pennsylvania*, 141 U.S. 18).

K. EXPRESS COMPANIES. — With express companies the same rule holds as with car companies. Where no specialized form of taxation has been adopted, the property tax is based on an assessment made on a unit basis of property or capital. A state board fixes the valuation and apportions to the State its proper share on the mileage basis, considering mileage run by the express cars. This method was upheld in the famous case of *Adams Express Co. vs. Ohio State Auditor* (165 U.S. 194). There the court held that "The States through which the companies operate ought not to be compelled to content themselves with a valuation of separate pieces of property disconnected from the plant as an entirety." Oregon is the newest convert to this now familiar doctrine.

L. TELEGRAPH AND TELEPHONE COMPANIES. — The tendency with telegraph and telephone companies is toward the assessment of capital stock. For valuing capital stock all property both tangible and intangible is now considered in the more progressive States. In apportioning interstate values to a State and interstate values to the local districts, miles of wire is the usual basis, with number of instruments coming in for some share of attention (125 U.S. 530, 141 U.S. 40).

M. FRANCHISES. — In New York the Ford Franchise Law provides that franchises shall be assessed as real estate. This was the position taken by Governor Theodore Roosevelt of New York in 1899 (Special Message, May 22, 1899). Other States consider franchises as personal property. Still others frankly do not consider them at all, shutting their eyes to the existence of this troublesome species of property. This method is happily passing.

Exactly what a franchise is is a point that has not yet been settled. But that it is a taxable piece of property is established. States applying the property tax or no tax at all to franchises can learn one lesson in assessment from Illinois, since the rule of assessing franchises here is the commonest one known. They had very conspicuous and substantial success in reaching this class of property which is sometimes complained of as being "as invisible and intangible as the soul in a man's body." The Illinois law requires the State Board of Equalization, in valuing the capital stock of corporations, to determine the "fair cash value of such capital stock, *including the franchise* over and above the assessed value of the tangible property of such company or association." The board is to adopt proper and just rules for this purpose. The meaning and intent of the law is plain here. And yet for a period of twenty-three years the board failed to assess a single dollar on the franchises of the railroads of the State. The Chicago Teachers' Federation in 1899 took up the matter of assessing franchises of the public service corporations of the city of Chicago. At that time there were twenty-three companies operating street railways, gas, telephone and electric light plants. Their franchise value was ascertained to be \$235,829,567, arrived at as follows: The actual cash market value of their stock was \$183,885,812; of their bonds was \$84,222,500; and hence the total value, stocks and bonds, \$268,108,312. At the same time their real estate and personal property was worth only \$32,278,745. The difference between these two sums, \$235,829,567, was the franchise valuation, illegally omitted from assessment. The Chicago teachers brought suit against the state board to compel it to do its duty, the action beginning in the lower court in Sangamon County, November 22, 1900. The decision being in favor of the teachers, the case was immediately taken to the Supreme Court of the State and this court affirmed in every particular the judgment of the lower court. The state board was ordered to make the assessment and did make the assessment.

The newer States of the Northwest are largely in the position of Illinois prior to 1900.

III. GENERAL METHODS OF ASSESSING AND EQUALIZING

A. LISTING. — Much variation is shown in the matter of listing property. New York has the shortest list of personalty — one item. New Hampshire has a short, simple list of items which commends itself. Wisconsin too has a short list, containing eighteen items. Indiana represents the other extreme, listing one hundred separate items, running all the way from No. 1, "Money on hand," to No. 100, "Female dogs owned or harbored." Kentucky likewise has one hundred items, beginning with bonds and ending with dogs over four months old. The average state list runs from twenty to forty items.

Wyoming Plan. — Wyoming has a schedule containing not only the usual items of personalty, but in the case of livestock, the valuation also. Thus, under cattle, using their 1905 form, "dairy cattle all ages" are assessed at \$25 per head; "bulls" \$40; "range cattle, calves counting yearlings," \$8. This classification scheme covers horses, mules and asses, sheep, goats and swine. If the assessor finds one burro, for instance, he will list it at \$5. Nevada has a plan similar in principle. The State Board of Assessors (composed of the fourteen county assessors) meet at the Capitol and fix certain valuations for the entire State. In their 1906 meeting, for instance, we find the following:

"Horses and mules,"	"left to each assessor."
"Beef cattle"	\$25 a head.
"Sheep"	\$3 a head.
"Hogs"	"left to assessor."
"Telephone lines,"	"left to assessor."

They use their own judgment as to what value to fix collectively. Valuations thus fixed are supposed to be actual cash values, and they cannot be altered by any county assessor.

Time. — The time of listing varies in a surprising degree even among neighboring States where similar conditions prevail. Thus Kansas lists property as of March 1, Nebraska as of April 1, Arkansas June 1, Louisiana uses April 1, Missouri June 1, and Texas January 1. Massachusetts dates her assessment May 1, while her neighbors, Connecticut and Vermont, have October 1 and April 1 respectively. This variation gives the

owner of certain kinds of movable personalty a good opportunity to escape assessment entirely, and with ease, if he lives near the state line. (For list of States and dates of assessment see Part VI, Table I.)

Assess at Full Value? — Most of the States require and emphasize the requirements that the assessment must be at the full cash value. Of course the requirement is seldom met. However, the supine attitude of Iowa and Illinois in this matter is surprising. The Iowa law (sec. 1305 code) provides, "all property subject to taxation shall be *valued* at its actual value, which shall be entered opposite each item, and shall be *assessed* at 25 per cent of such actual value." Illinois makes it 20 per cent.

B. REASSESSING. — Wisconsin provides that where the assessment made by local assessors is not in substantial compliance with law, and public interest requires a reassessment, the State Tax Commission may order a reassessment of the districts at the districts' expense.

C. TAX FERRETS. — Ohio and Iowa have long been the home of the tax ferret. This plan of hiring an inquisitor on the commission basis to ferret out tax dodgers has accomplished some temporary gains and produced some permanent losses. Kansas has recently tried the plan, where it has been pronounced by capable observers "a social crime." Tennessee is the youngest offender in this tax inquisitor system.

D. PUBLISHING ASSESSMENTS. — On the theory that the public business demands publicity, many localities are now publishing a complete list of taxpayers and their individual assessments. Illinois has used this plan since 1897. Rhode Island requires it in her law. Delaware likewise uses the system to some extent. A few towns in New Hampshire have issued such a publication in neat pamphlet form. Nevada requires this list for every county.

E. EQUALIZING. — Local boards review the assessors' lists and attempt to overcome the evils therein by "equalizing." But this equalizing not only does not equalize but cannot equalize. Here it is a good thing to look at local government actually at work; to either attend the meetings of these local boards, or read the minutes of such meetings. I have carefully

gone through the reports for one county in North Dakota, twenty-eight township boards reporting. And in all these twenty-eight townships there was but one person appearing before the board to complain. His grievance was that his land was assessed too high. The complaint was not granted. No one else appeared, for nobody knew his neighbors assessment, and consequently everybody was entirely in the dark concerning the equity of his assessment. To redeem these meetings from being solemn farces they do make some rough "equalizations," unasked, as their sentiments prompt them. To illustrate, take these three cases, selected from the manuscript minutes of the North Dakota county referred to.

(1) "Moved by D. McVeon, seconded by Henry Halleck, that two sheep be taken off from O. H. Brenna Personal Property tax list, valued at \$2, on account of having died lately.

"Motion carried."

(2) "Moved and carried that one wagon be taken off from Gunder Jacobson's property list, valued at \$5, on account of not being worth anything."

(3) "Moved . . . that one two-year-old horse, valued at \$14, be taken off Henry Strond's assessment list, on account of having died from poison."

While there is no doubt about the justice and human kindness of these changes, they hardly scratch the skin of the real inequalities of assessment in the township. In one of these townships, for instance, a piece of real estate sold for \$16,000, but was assessed at \$1500, at the same time a small neighboring piece was bought by a humbler man for \$75 and assessed at \$90. These defects the board does not cure. Prevention, rather than cure, is the solution.

IV. THE ASSESSOR

A. How CHOSEN. — The manner of choosing assessors is still an unsettled problem. States that appoint are chafing under the system. South Dakota (1905) in despair exclaims, "All assessment should be in the hands of the state board, which should appoint every assessor in the State." Arizona's governor (1903) recommends that the office of assessor be made *elective* instead of appointive. Missouri is trying the county assessor,

elected for a term of four years. Louisiana wearied of her appointive assessors, and the new law (1906, Chs. 8, 63, 78, 182) provides for their election. Some States have made the assessor ineligible to reelection. One lesson is evident in all this, and that is this, — the local assessor, when left to himself alone, will not meet the difficult requirements of his office, no matter how he is chosen. His official conduct must be standardized by some outside contact in the form of central supervision.

B. TERM, PAY. — Assessors have terms varying from one to four years. The long term is better, for then they can make use of what little expert knowledge they have acquired by their experience. Kentucky and several Southern States pay the assessor a certain per cent of his assessment returns, thus offering him a financial inducement to boost his returns. The more common method is the per diem allowance for country work, and too small an allowance too, considering the importance of the work. Cities pay by the year. Thus Philadelphia has a Board of Revision of Taxes composed of three persons whose salaries are \$6000 each. In their department they have a force of thirty-one clerks who handle the work of the office, together with sixty-six assessors with a salary of \$2000 each.

C. UNIT, TOWN OR COUNTY. — In New England, of course, we find the town unit for the local assessor. All the new Northwest has made the county the local unit. The following States also have adopted the county as their assessment unit: Illinois, Indiana, New Jersey, Florida, West Virginia, Virginia, North Carolina, Alabama, Nebraska, Kansas, and Missouri. The county assessor usually appoints one deputy or assistant in each town. This is no doubt one step ahead of the unsupervised town assessor plan.

D. SUPERVISION. — Some supervision from without the county is needed. The county system, when tried alone, has already failed. A Connecticut Tax Commission reported in 1868, concerning decentralization, "One of the obvious and peculiar defects of our system is, that it has no central or supervisory head by which to secure any sort of uniformity in the manner or efficiency of its administration." Kansas illustrated this evil before adopting her present centralized scheme of county assessor under the State Tax Commission. Under the old régime

township assessors met at the courthouse in the spring, there to agree on an "equal basis of valuation," which basis in any and all events was to be the actual cash value. A visitor at one of these meetings writes that the "assessors openly stated that they would not pledge themselves to assess at any fixed ratio, as they knew that some of the other assessors would assess at a less ratio than that which was adopted, whatever that might be. Harmony was finally attained by the passage of a resolution to assess at the usual ratio, and a general laugh followed the inquiry by one innocent member as to what that ratio was. No one seemed able to answer" (Kans. 13 Bur. Labor).

Wisconsin has, perhaps, worked out as perfect a system of local government and administration in tax affairs as the United States has yet seen. It is a chain of three links — the State Tax Commission, the County Supervisor of Assessment and the Local Assessor. On the side of administration, it is the American ideal combination of bureaucracy and democracy. The State Tax Commission is a body of three men, appointed for a long term, eight years, at a good salary, \$5000. The office, thus dignified, has been filled, German-fashion, with thoroughly equipped persons. It is bureaucratic. The county supervisor is nearer the people, being chosen by the county boards, with powers advisory and supervisory merely. He is the middle link in the chain. The local assessors are elected by the people of the town. They are purely democratic. The supervisors meet at the State House in the spring, with the State Tax Commission. After a two or three days' session, they return to their respective counties, knowing the law and their duties clearly. They call meetings of the local assessors and see that they too know the law and their duties. They then take the field with the local assessors and see that the work is done according to law. They can begin ouster proceedings against a recalcitrant local assessor, or they can inaugurate a movement for a reassessment at the district's expense. Their real work, however, is thoroughly peaceful and sympathetic, being largely educative in nature.

Other States have systems approaching close to this, notably Indiana. But in no other case has the experiment been made so seriously and so thoroughly. It has been in force six years.

The first two years showed stupendous gains; the last four have not been so good. There has been a little retrogression. But they are still pressing the assessors from above to go on with energy and courage! Students of tax literature are referred to the excellent reports of the Wisconsin Tax Commission, and especially to the "Proceedings of the Annual Meetings of the Supervisors of Assessment."

V. SUMMARY AND RECOMMENDATIONS

Assuming that the general property tax is to linger a while longer, I venture to give a brief summary of what has been said in this paper, and to offer some recommendations. These will be given, not in any way to help perpetuate the general property tax, but to help make an easy transition to something better.

A study of methods of assessment reveals the fact that, with the exception of real estate, assessment now has become almost entirely a matter of self-assessment. Although methods vary in detail from State to State, they come back to the same self-assessment in the end. The time of assessment, too, varies in a remarkable way without any apparent good reason. A study of the defects and shortcomings in present-day methods of assessment makes one rather pessimistic. Democracy has certainly failed here, if this is a fair sample of administration. Oaths and penalties have been tried in vain. Only occasionally now do we read in a governor's message the belated recommendation that the oaths and penalties be made more severe. Tax ferrets have been tried without success. Electing and choosing assessors have failed to give the assessor any more brains or backbone. He still remains at the center of the problem. Whether the general property tax stand or fall, it must ultimately depend on this local assessor. If this tax can possibly be made a success, as the Oregon Commission believed it can, then it will doubtless be continued. If it cannot be made a success, of course it will be abandoned. It was pointed out that Wisconsin has gone the farthest of all in her intelligent effort to make a success of assessment under this tax system. Yet Wisconsin has only had two thirds success.

Some able writers on taxation have said that you cannot improve the general property tax, for the more you improve it

the worse you make it. However, methods of assessment can at least be purged from some of their grosser evils. And with this hope in mind, rather than any expectation of suggesting an ideal system of assessment, I make the following recommendations:

RECOMMENDATIONS

- I. State Constitutional Limitations, requiring "Uniformity."
This should be amended. The correct form is found in the new Oklahoma constitution, section 5. It reads, "Taxes shall be uniform *upon the same class of subjects.*"
- II. The Assessment.
 1. Assess at the same date in all the States.
 2. Assess land and improvements thereon separately.
 3. Assess personal property annually; real estate once every five years.
 4. Provide a space on the assessor's blanks for entering the item "Amount insured for," after certain forms of personalty.
 5. Assess corporations as business units.
 6. Provide for reassessment at expense of local district in case original assessment is not according to law.
 7. Publish the assessment list, showing each taxpayer's name and assessment.
- III. The Assessor.
 1. Provide for centralized supervision. The Wisconsin three-link system of state board, county supervisor and local assessor is here recommended.
 2. Elect local assessor. To preserve our traditional democratic scheme of local government, it is recommended to continue the election of town assessors, under the expert supervision mentioned above.

TABLE I

*List of States with Date of Assessment and Frequency of
Assessing Real Estate*

STATE	DATE OF ASSESSMENT OF PROPERTY	YEARS' INTER- VAL IN ASSESSING REAL ESTATE
Alabama	October 1	1
Arizona	First Monday in February	1
Arkansas	June 1	2
California	First Monday in March	
Colorado	April 1	
Connecticut	October 1	1
Delaware		
Florida	January 1	1
Georgia	March 31	1
Idaho	Second Monday in January	
Illinois	April 1	4
Indiana	March 1	4
Iowa	January 1	2
Kansas	March 1	2
Kentucky	September 1	1
Louisiana	April 1	1
Maine	April 1	1
Maryland		
Massachusetts	May 1	1
Michigan	Second Monday in April	1
Minnesota	May 1	1
Mississippi	February 1	4
		(1900 and after, only 2)
Missouri	June 1	1
Montana	First Monday in March	1
Nebraska	April 1	4
Nevada	January 1	1
New Hampshire	April 1	1
New Jersey	May 20	1
New Mexico	March 1	1

TABLE I—*Continued*

STATE	DATE OF ASSESSMENT OF PROPERTY	YEARS' INTER- VAL IN ASSESSING REAL ESTATE
New York	May 1	1
North Carolina	June 1	4
North Dakota	April 1	1
Ohio	Sunday before second Monday in April	10
Oklahoma		
Oregon	March 1	1
Pennsylvania		
Rhode Island		
South Carolina		
South Dakota	May 1	1
Tennessee	January 10	1
Texas	January 1	1
Utah	January 1	1
Vermont	April 1	4
Virginia	First Monday in February	1
Washington	March 1	
West Virginia	April 1	1
Wisconsin	May 1	1
Wyoming	April 1	1

TABLE II

Supervision of Assessment and Taxation by the States. A
List of the States and the Officers Relating to Taxation.

ALABAMA: The state auditor.

The state board of assessors for railroad, telegraph and telephone companies, composed of the governor, the secretary of state, the auditor and the treasurer, together with the attorney general, who acts as adviser and decides any tie vote.

The state tax commissioner, appointed for four years by the governor, and the district (county) tax commissioners, appointed for four years by the state tax commissioner and commonly known as the "back tax commissioners."

ARIZONA: The auditor and two other members appointed by the governor for a term of two years, who constitute the territorial board of equalization; they also constitute the board of assessment of railroad property.

The territorial auditor, appointed by the governor.

ARKANSAS: The auditor of the State, elected for two years. The state board of railroad commissioners, composed of the governor, the secretary of state and the auditor of state.

CALIFORNIA: The state board of equalization, which assesses certain railroad property and equalizes assessments between counties, and is composed of the state comptroller and four members elected by districts.

The state comptroller, elected for four years.

COLORADO: The state board of equalization, composed of the governor, state auditor, state treasurer, secretary of state and attorney general.

CONNECTICUT: The state board of equalization, composed of treasurer, comptroller and tax commissioner.

DELAWARE: The state treasurer, elected for two years.

FLORIDA: The comptroller, elected for four years.

GEORGIA: The comptroller general.

IDAHO: The state board of equalization, composed of the governor, secretary of state, attorney general, state auditor and state treasurer.

ILLINOIS: The state board of equalization, one member from each congressional district, elected for four years, together with the auditor of public accounts.

The auditor of public accounts.

- INDIANA:** The state board of tax commissioners, three persons appointed by the governor for a term of four years, together with the secretary of state and the auditor of state.
- IOWA:** The state executive council, composed of the governor, secretary of state, which constitutes the state board of review, and acts as a state board of equalization, and also as an assessment board for certain classes of property.
- KANSAS:** The state auditor.
Tax commission consisting of three men appointed by the governor for a term of four years.
- KENTUCKY:** The state board of equalization of assessments, composed of one person from each appellate district in the state, appointed by the governor, together with the auditor of public accounts. The term is two years.
- LOUISIANA:** The state board of appraisers, composed of the auditor and one member from each congressional district, appointed by the governor, treasurer, attorney general and secretary of state, which assesses the property belonging to corporations, associations and individuals employed in railway, telegraph, telephone, sleeping car and express business.
State board of equalization, composed of one member from each congressional district, elected for a term of four years.
This board equalizes assessments of all real and personal property.
- MAINE:** The board of state assessors, consisting of three members chosen by the legislature for a term of six years, one elected every two years. This board has supervision over the local assessors, acts as a board of equalization, and administers the laws as to the taxation of corporations.

- MARYLAND:** Assessors at large, appointed by the governor, two for each assessment district of the county. State tax commissioner, appointed by the governor, comptroller and treasurer for a term of four years.
- MASSACHUSETTS:** The state auditor of accounts, elected annually at the state election.
The state tax commissioner, appointed by the governor for a term of three years.
- MICHIGAN:** The state board of equalization, consisting of the lieutenant governor, the auditor general, the secretary of state, the state treasurer and the commissioner of the land office.
The state board of tax commissioners, created in 1899, formerly of three, now of five members, appointed by the governor for a full term of six years.
- MINNESOTA:** The state tax commission (the Minnesota Tax Commission).
- MISSISSIPPI:** Railroad commissioners, elected for four years, who act as state railroad assessors.
- MISSOURI:** State revenue agent, elected for four years. State board of equalization, consisting of the governor, state auditor, treasurer, secretary of state and attorney general.
State tax commission, three persons appointed by the governor.
- MONTANA:** State board of equalization, composed of the governor, secretary of state, state treasurer, state auditor and attorney general.
- NEBRASKA:** State board of equalization, composed of governor, auditor of public accounts and treasurer.
- NEVADA:** State board of assessors, composed of the county assessors in session at the Capitol, governor of the State as chairman. They assess public service corporations, and certain kinds of personalty.
State board of revenue, consisting of governor, comptroller and attorney general.

NEW HAMPSHIRE: The state board of equalization, consisting of five members appointed by the supreme court and commissioned by the governor, and acting as board of assessment for certain classes of property.

NEW JERSEY: State board of taxation, composed of four members appointed by the governor, no more than two to be of the same political party.

NEW MEXICO: Territorial board of equalization, composed of one taxpayer appointed by the governor from each of the five judicial districts.

NEW YORK: The state board of tax commissioners, of three members, appointed by the governor, to hold office for a full term of three years, one member retiring each year.

The state board of equalization, composed of the commissioners of the land office and the commissioners of taxes.

State comptroller and state treasurer, elected for a term of two years.

NORTH CAROLINA: Board of state tax commissioners, composed of the board of corporation commissioners, which exercises general supervision over tax lists and assessing officers, and is required to make an annual report to the governor.

Corporation commissioners and board of state tax commissioners are to be a board of appraisers and assessors for railroad, telegraph, telephone, street railway, canal, and steamboat companies, and other companies exercising the right of eminent domain.

NORTH DAKOTA: State board of equalization, composed of governor, state auditor, state treasurer, attorney general and the commissioner of agriculture and labor.

OHIO: State auditor.

The state board of appraisers and assessors, composed of the state auditor, state treasurer and attorney general.

The decennial state board of equalization of real estate, composed of as many persons as compose the state senate, and elected from the senatorial districts.

The annual state board of equalization for banks, composed of the governor, the attorney general and the state auditor.

The annual state board of equalization for railroads, composed of the state auditor, the commissioner of railroads and telegraph lines, the attorney general and the state treasurer.

OKLAHOMA: (New constitution not yet ratified.)

State board of equalization consisting of the governor, state auditor, state treasurer, secretary of state, attorney general, state inspector and examiner, and president of the board of agriculture.

Corporation commission, assessment of property and the appraisement of their franchises for taxation of all transportation and transmission companies.

OKLAHOMA: (Territorial.)

Territorial board of equalization, composed of the governor, territorial auditor and secretary.

OREGON: None (county officers).

PENNSYLVANIA: State board of revenue commissioners, composed of the auditor general, treasurer and secretary of the commonwealth.

RHODE ISLAND: General treasurer of the state, elected every year.

SOUTH CAROLINA: Comptroller general, elected for a term of two years.

State board of assessors, composed of the treasurer, secretary of state, comptroller, and attorney general and chairman of the railroad commissioners.

State board of equalization, composed of members elected by the county boards of commissioners.

SOUTH DAKOTA: State board of equalization, composed of the governor, auditor, secretary of state, treasurer and commissioner of school and public lands.

TENNESSEE: State board of equalization, composed of the secretary of state, treasurer and comptroller of the treasury.

Revenue commissioners, three in number, elected every two years by the quarterly courts, one of whom is to be an expert accountant. They are to inspect reports and examine accounts.

Revenue agents, three in number, appointed by the comptroller for a term of two years. They are to examine the records of collections and disbursements, and may also bring suit against delinquent officers and corporations.

State tax assessors, commonly known as the railroad commission, three freeholders, appointed by the governor biennially.

Board of equalization of railroad assessments, composed of the governor, treasurer and secretary of state.

TEXAS: Comptroller of public accounts.

Board of equalization for unorganized counties, consisting of the governor, attorney general and secretary of state.

UTAH: State board of equalization of four members, appointed by the governor for a term of four years.

VERMONT: The commissioner of the state taxes, who administers the state taxes on corporations, appointed biennially by the governor.

VIRGINIA: Auditor of public accounts, elected for two years.

Board of public works, consisting of governor, auditor and treasurer of the commonwealth, which formerly (before 1902) assessed the railroads, and performed certain other duties connected with taxation.

By the constitution of 1902 there was established a state corporation commission, composed of three members appointed by the governor for six years to take the place of the board of public works.

WASHINGTON: State board of equalization, composed of the secretary of state, the commissioner of public lands and the auditor of state. (Since 1905 also the three members of the tax commission.)

An advisory state tax commission of three members (created by the legislature of 1905).

WEST VIRGINIA: The board of public works, consisting of the governor, the attorney general, the superintendent of free schools, the auditor and the treasurer, together with the secretary of state *ex officio*, forms a state board of assessment.

The state board of equalization, authorized by the legislature at each decennial assessment of real estate.

State tax commissioner, appointed by the governor for six years.

WISCONSIN: State tax commission, composed of three tax commissioners, appointed by the governor for eight years.

WYOMING: State board of equalization, composed of the secretary of state, treasurer and auditor.

THE HABITATION TAX

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ADDITIONAL sources of public income are essential to modern efficient government. This is due to the great demand for increased revenue, and the need of a substitute for the general tax on personal property. The growth of urban population has made necessary additional taxes. A city government is more costly than governments of purely rural communities with their freedom from sewer, water, lighting and police expenses. The increase of taxation that has to be borne by the city dwellers falls primarily on property within the corporate limits. In theory, all taxation in modern cities is levied on the real and personal property therein, but in reality, the tax is very largely contributed by the realty. It is well known that personal property everywhere does not contribute its share of taxation. Hence, in the selection of new sources of taxation, efforts should be made to relieve real estate as much as possible from the undue proportion of taxation which it now bears by securing from the owners of personalty the proportion of tax which they ought in equity to pay. The complications in the present method of assessing personal property render evasion easy and justice impossible. The new methods should conform as nearly as possible to the established principles of taxation. The more important of these principles are the following:

1. A tax should be levied according to the ability of the taxpayers to contribute. This principle is so obvious that it needs no discussion. The other theories of taxation, such as benefit and sacrifice, seem to have been largely abandoned, and ability accepted as the fundamental principle.

2. Again, a tax should be certain both as to its amount and payment. The amount to be paid should be definitely known both to the taxpayer and to every one else in the same community.

3. A tax should be so contrived that its assessment and collection may be made with a minimum of expense. Its levy should be simple, requiring no detailed inquisition into the affairs of the taxpayer, as this will tend to deprive it of public support by affording apparent justification for its resistance.

These are the principal canons of taxation laid down by Adam Smith, and if carefully followed, undoubtedly furnish the basis of an ideal revenue system.

As a substitute for the tax on personal property, the tax on rentals, or "Habitation Tax," as it has been called, has been recommended as conforming in large measure to the above principles. This is a tax levied upon the occupier of residences according to the rental value of the places they occupy. In order to attain substantial justice, the rentals of property below a certain amount are exempt from the tax. This exemption is felt to be necessary because the smaller properties are now bearing far more than their proportion of taxation, and again, a certain amount must be expended for subsistence before any considerable degree of taxpaying ability emerges. In the more recent proposals of this tax, it applies only to the rentals of buildings occupied as dwellings. Business properties are exempt. It is felt that such buildings are effectively reached by other kinds of taxes.

This tax is not proposed as a sufficient source of revenue. From a financial point of view it is defective in elasticity as are all taxes levied at a flat rate upon property which does not vary greatly from year to year. It is therefore necessary to provide in some of the other taxes for the variations to be introduced as the fiscal needs change. This should not be omitted, as an unelastic system of taxation, by bringing in a surplus of revenue in prosperous years, may lead to extravagant undertakings and unwarranted expenditures on the part of the legislators, and it is wise to shield them from the temptations of an overflowing treasury.

The habitation tax is brought forward as a supplemental tax to serve as a part of a general system. It is offered as a substitute for the tax on personalty, and it is believed to contain features that will make it adaptable to modern conditions and various localities with a minimum of friction.

Theoretically, the income tax is regarded as approaching most nearly to the principle of ability, and for a number of years this tax has been expected to furnish the means of escape from the inequalities in the taxation of general property. Increasing study of the abuses inherent in the practical operation of the income tax in those countries where it has become a settled part of the fiscal system has weakened the faith in the efficiency of this tax to reach considerable classes of personal property. When the income tax is applied on the principle of stoppage at source, — taking the tax out of the dividends before they are paid to the stockholder, — it has proven successful. Its greatest defect is in the fact that it must rely upon the declaration of the taxpayer as to the amount of his income derived from investments in notes, mortgages, bonds and other securities to which the principle of stoppage at source cannot be applied. In the ascertainment of this part of the income, the tax has become subject to abuse. In so far as the income tax is successful, much the same result is now obtained in some of the American States by the use of corporation taxes. Thus, while the practical results of the income tax are secured in the taxation of corporate property, the tax on rentals has been proposed in the endeavor to reach that species of property not effectively reached either by taxes on income or corporations.

The expenditure for house rent is generally some indication of the occupant's income. It is true it is not an absolute measure of income, but in a general way differences in rent tend to approximate differences in taxpaying ability. Normal persons are fond of material comforts and luxuries, and an increase in income generally expresses itself at once in larger and more elaborate homes. It is also claimed that the habitation tax reaches funded income and taxes it at a higher rate than income from services such as the income of lawyers and physicians.¹

In all schemes of income taxation an effort is made to make this discrimination so as to avoid the hardship in taxing income from service at the same rate as income derived from government bonds or other permanent investments. The tax on rentals, it is said, reaches income from investments and taxes it at a higher rate than income from service because, in so far as the

¹ Leroy-Beaulieu, "*Traité de la science des finances*," Part I, Book II, Ch. 7.

residence is the index of income, it is likely to vary with the amount of wealth, and, in consequence, those persons having an income from investments in government bonds and other securities, and with a reasonable assurance of its permanence, will have more elaborate habitations than those obliged to secure an income from their personal services, for the latter will of necessity feel themselves obliged to save a part of their earnings. Hence they will not be able to spend so much on a habitation. Thus it seems the tax on rentals taxes the income derived from invested funds at a higher rate than that derived from service and so conforms to the ideal scheme of an income tax.

In the French cities where the tax on rentals is in operation a progressive scale has been adopted. The houses are classified according to their rental value. As a rule those with a rental below five hundred francs are exempt. The rates on the other classes vary from year to year according to the fiscal needs of the community.¹

In defense of this progression it is said that the lower in the social scale you go the higher is the proportion house rent bears to the total expense or income. The poor spend a much larger proportion than the rich for the rent of their homes. It has been claimed that a progressive rate of taxation on rentals would counterbalance the decreasing proportion rent bears to the total expense. While there is truth in this, it should be remembered that expenditure is only an approximate measure of a man's income or ability to pay taxes. In a country like the United States, where the democratic ideal is strongly emphasized, the amount of rent paid is a more uncertain index of income than in countries where social classes are more sharply defined. This is especially true of the middle and lower middle classes. However, this objection to the progressive feature becomes

¹ In the year 1890 the following rates prevailed :

Rentals to 599 francs	6½%
Rentals to 699 francs	7½%
Rentals to 799 francs	8½%
Rentals to 899 francs	9½%
Rentals to 999 francs	10½%
Rentals above 1000 francs	11.74%

^a"Dictionnaire des finances," Leon Say, Vol. II, p. 854. Given in Seligman, "Progressive Taxation," p. 56.

less serious if the rental exempted from taxation is reasonably large.

The two principal criticisms of the habitation tax are the following: First, it would not reach the rich bachelor, who as a rule does not maintain an expensive residence. Second, it would tend to put an additional burden on persons with large families.

It is true this tax would not reach rich bachelors in the same degree as persons of family. A bachelor may be a boarder in the family of a much poorer individual whose rent is large enough to render him liable to the habitation tax. Probably the best method of meeting cases of this kind is to rely upon the inheritance tax. On the assumption that those not reached by the habitation tax are enabled to accumulate more wealth, the death duty will make up for the loss by the tax on rentals. As to the second objection, a scale might be adopted by which the size of the family would be taken into consideration and the rate of taxation adjusted in such a manner as to give the heads of the larger families the benefit, and place an additional burden upon those smaller households desiring to maintain expensive establishments. It would not be difficult to lower the rate of taxation somewhat in cases in which the family exceed a certain number, or to exempt such families altogether. In Tasmania a reduction is made for each child. In this way the most serious objection to the habitation tax might be removed.

One of the latest proposals of this tax is that in the minority report of the New York Special Tax Commission of 1906. This recommends that the personal property tax be abolished and the tax on rentals substituted. It proposes to levy the tax at a graduated rate. The sum to be deducted from the total rent before the tax was to be imposed varies according to the size of the cities.

In cities of the first class (250,000 inhabitants or more), \$600; in cities of the second class (50,000 to 250,000 inhabitants), \$400; in cities of the third class (under 50,000 inhabitants) and in incorporated villages, \$200; in towns and unincorporated villages, \$100.¹ This variation in the amount of exemption is an attempt on the part of the committee to adjust the tax in some degree to the differences in rents which exist in the dif-

¹ Report of New York Special Tax Commission, 1906, p. 172.

ferent cities of the State. Rents are higher in New York City and Buffalo than in the other cities and smaller towns.

The rates of taxation recommended by the New York Commission are interesting as showing the graduation. They are as follows:¹

RENTAL	RATE OF TAXATION
\$2000 or less	3%
\$2000 to 5000	5% on excess above \$2000
\$5000 to 10,000	10% on excess above \$5000
\$10,000 to 20,000	15% on excess above \$10,000
\$20,000 and over	20% on excess above \$20,000

A habitation is defined as a building or part of a building used as a place of abode by one or more persons forming a single household and such other buildings in connection therewith as are used for the purpose of residence, but not such buildings or parts of buildings used for business purposes. Different parts of buildings, rooms or suites of rooms in hotels serving as places of abode for guests or lodgers having no households, are considered as habitations for the purpose of taxation. "Occupant" is defined as a person who as head of a household occupies a place of abode within the meaning of this article for a period of three months of the preceding year either for himself or for his family or dependants or boarders or lodgers. The liability to the tax after a three months' occupation is designed to reach that considerable class of persons which possesses residences in the summer and winter resorts of the country.

The New York commissioners, in recommending the tax on rentals, did not urge its adoption as a law applying to the entire State regardless of the desires of the local units. The bill which they propose provides that the board of supervisors of any county or the common council of any city may exempt from taxation the personal property within the limits of such county or city and substitute the tax on habitations. This is the local option feature, and is considered wise, as it is possible that many of the local units in which wealth is more evenly distributed would prefer to continue the assessment of personal property by the general property tax. The general property tax on personalty is not the failure in the rural districts that it has become elsewhere.

¹ Report of New York Special Tax Commission, 1906, p. 172.

The local option feature of the proposed law is especially wise in the present state of public opinion. It is most unlikely that any legislative body will soon adopt what seems so radical a form of taxation if it is to apply at once to the entire State. If, however, the bill has the local option feature and will not go into operation anywhere until it has been adopted by the local legislative body, it is quite possible that the state legislature might much more easily be induced to consider it. This was the manner in which the tax was introduced in Montreal. The charter made the tax permissive, and the council decided to adopt it.¹ Altogether, the proposed habitation tax as recommended by the minority of the New York Commission represents perhaps the most scientific development of the idea of this kind of taxation. The commissioners deserve great credit for the skill with which they have worked out and presented their plan.

One of the great advantages of this kind of taxation is the large increase in revenue that could easily be made to follow its adoption. The anticipated increase in revenue is set forth by a table in the report of the minority of the New York Special Tax Commission of 1906. This table is made up of actual figures taken from the assessors' rolls and shows the increase in revenue that might be secured. In the table the rental is estimated at 8 per cent of the assessed value of the premises.²

NOMINAL DESIGNATION	PERSONAL ASSESSMENT	VALUE OF RESIDENCE (Land and Building)	PRESENT TAX ON PERSON- ALTY	TAX UNDER NEW LAW
A	\$300,000	\$1,600,000	\$4,436	\$22,792
B	150,000	2,745,000	2,218	40,112
C	100,000	1,200,000	1,478	17,392
D	50,000	765,000	739	10,442
E	50,000	490,000	739	6,032
F	100,000	590,000	1,478	7,532
G	1,000,000	3,000,000	14,780	46,192

¹ Charter of the City of Montreal, 1899, Article 363. Quebec, 62 Victoria, Ch. 58.

² Report of New York Special Tax Commission, 1906, pp. 53-54.

From this table it is clear that these wealthy taxpayers would pay by this tax from three to twenty times the amount they are now paying in personal taxes. The wealthy resident whose intangible personal property now so largely escapes taxation would be reached, and the exemption of the lower rentals from the tax would relieve the tenement house population and also the large class of persons whose rents are so considerable a part of their expenses of living. At the same time the revenue derived would greatly exceed that which is now yielded by the tax on personalty.

Another advantage of the habitation tax as a tax on income not reached by the corporation taxes is that it will fall on those most able to bear it and who now in great measure evade the general tax on personal property. It has been shown that the tax upon the rental value of property cannot be shifted, but falls upon the occupier alone save under exceptional conditions.¹ Thus, this tax on rentals would reach the class desired to be reached and would have to be borne by them alone; namely, the class occupying the more expensive kinds of dwellings. As the tax falls upon the person paying the rent, it cannot be said to be an additional burden placed upon real estate. In those cases in which the owner is also the occupier, the tax may be regarded as a tax on the funded income of those not reached by other taxes. The general effect would then be to lessen the tax burden now levied on real estate.

One of the greatest problems of modern finance is to lighten the burden of local real estate taxation. Owing to the evasions of the personalty owners and their escape from the assessor, the tax needed for local purposes, and in most States, state revenues as well, has to be levied very largely on the owners of real estate. The increased demand for urban residential property enables these owners to shift a large amount of the tax to the tenants, and hence the high rents. In so far as the habitation tax as recommended by the minority of the New York Commission might be made to produce a considerable revenue for local purposes, it is inevitable that the tax on real property would be lessened and in consequence rents would fall. The social and industrial advantages of a change of this kind would be very

¹ Seligman, "On the Shifting and Incidence of Taxation," p. 127.

great, since rent is so important a factor in increasing the congestion of population.

The habitation tax conforms in a high degree to the principle of certainty that has already been laid down. If a person does not change his residence, and if the rate of tax on rentals is not changed from year to year, each taxpayer in the community knows what his tax will be and also what the amount is that each of his neighbors will have to pay as the rent of buildings is usually fairly well known.

At the present time much of the lack of interest in the problems of taxation and the consequent slowness of reform in this kind of legislation are due to the utter ignorance of the citizens of the local units as to the amount of tax which their neighbors pay. Save in the rural districts, few taxpayers know what the assessment is of the property adjoining their own, and they are much less likely to know the amount of personality assessed to the citizens of their community. Publication of the assessors' rolls in the newspapers would certainly quicken interest in questions of taxation, whatever might be the other results.

There are two reasons why the habitation tax would not cause much friction in its operation. One is the ease with which it might be assessed and the impossibility of deception, and the other is the absence of anything in the nature of an inquisition into the affairs of the taxpayers. These are advantages of no slight importance.

In placing a tax on rentals it is only necessary to know the amount of the rental, and this is more or less common knowledge in the entire neighborhood. If it is not, it is very easy to ascertain. The modifications of the tax that have been suggested as in the case of the change of the rate for bachelors and for families with numerous children are also changes that are dependent upon certain well-known or at least easily discovered facts. Hence, in the assessment of this tax there would be scant opportunity for deception or collusion, and no one could find fault with the amount levied upon his neighbor.

One of the very great advantages of this tax is that it does away with the necessity of inquiring into the affairs of the taxpayers and securing affidavits from them. In America one of the

government acts most resisted is the investigation of a person's private affairs. The absence of social classes and the teachings of more than a hundred years of democracy have developed a strong desire in our citizens to keep to themselves their own financial standing. Therefore, when the assessor demands from the taxpayer an inventory of his wealth, he is frequently met with a refusal or is given a statement far from the truth. The feeling that each person has the right to resist inquisition even on the part of the government is one of the chief reasons for the partial failure of the income tax in the older countries of the world and for its much more complete failure in the United States. This is meant to apply to the part of the income that is determined by the statements made by the taxpayer in his declaration. The tax on rentals is therefore in harmony with the feeling of resentment toward any inquisition into one's financial ability and would accordingly eliminate much of the friction now characteristic of the fiscal system.

It has been assumed that, as a general principle, taxes on consumption are bad, and this is perhaps true enough to make it a rule that such taxes should not be levied oftener than necessary. Other sources of revenue should be found whenever possible. However, consumption when thought of in this connection is assumed to mean consumption necessary to guarantee the welfare of the community. This is the kind of consumption in vogue when the earlier works on taxation were written and when therefore the principle above mentioned gained general acceptance. With the great increase of wealth in the past half century, however, and the keener competition among social classes, it seems that consumption has become a thing which it is not safe to use in judging the necessities of the people. It does not indicate expenditure for social welfare, but tends rather in many instances to show a desire to consume conspicuously and wastefully. Large classes in the community maintain great establishments not for the sake of necessity, but primarily for the sake of the social standing the maintenance of these households gives them. The sense of fitness conforms in considerable degree to the principle of conspicuous waste. In so far as this is true, the criticism of the habitation tax as a tax on consumption loses much of its force.

It is, perhaps, going too far to accept Wagner's theory that taxation is a certain socio-political instrument to be used for the conscious improvement of society,¹ yet it would seem that if the government is justified in levying some regulative taxes such as those on certain vices for the sake of control and repression, it is not doing violence to the imagination to think that wasteful consumption for the sake of display might possibly be considered as somewhat akin and properly subject to taxation. The tax on expensive habitations might have certain sociological results. In so far as its imposition would tend to check wasteful display in the maintenance of great establishments, it would tend to eliminate a conspicuous form of invidious comparison which at the present time is one of the chief factors determining men to erect immense habitations. A beautiful and expensive residence is a standing witness of the owner's ability to pay, and it at the same time clearly proclaims him in a different class from most of those who view it.

Again, in so far as the habitation tax would tend to reduce the number of magnificent residences, it would have the effect of decreasing the value of real estate and in this event a social gain would accrue to the modern city. The huge private parks surrounding so many of the fine residences in our cities might tend slightly to diminish in size, and in this way more of the working class might have homes in other places than the congested sections where they now reside.

If, then, the tax on habitations can be so arranged that it will not interfere with the amount of money that must be spent in order to secure for the people their actual welfare, but will only bear on that part of the expenditure which is unnecessary to the well-being of the community, the objections to it as a tax on consumption will in some degree be removed. If the exempted minimum rental is properly adjusted, there can be no serious complaint that such a tax will fall unjustly as a consumption tax upon those least able to bear it.

HISTORY OF THE HABITATION TAX

The tax on the rental values of property is not new. It had its beginning in the action of the Constituent Assembly of

¹ Wagner, "Finanzwissenschaft," Vol. I, § 27.

France in the year 1791. This assembly, erected upon the ruins of the French monarchy, sought to construct a new fiscal system that would eliminate the obnoxious features that had been so characteristic of the monarchy preceding. Of these one of the worst was the inquisition into the affairs of the citizens. In seeking, therefore, for new objects of taxation, and also such as would require no inquisition, the members of the Assembly resorted to the tax on rentals. Since that time this tax has prevailed in France though its strict theory is not carried out in all departments. In a number the tax is assessed upon the ability of the citizen to contribute and this ability is determined by the amount of his rent and also certain other evidences of financial standing.

In 1887 an attempt was made to modify the tax on rentals by increasing the progressive feature so as to enlarge the contribution in proportion to the amount of the rental, and although brought forward as a government measure, the bill was defeated. The scheme was ingeniously worked out by Dr. Koenig, and although failing to become a law, served to attract the attention of students to the possibilities of this tax.¹

The tax on rentals has been in force for a number of years in some of the German Cities, among them Berlin, Frankfort, Dresden and Strassburg. The proportion of the total revenue furnished by the tax is shown by the following table:²

CITIES	PER CENT OF ALL TAXES
Berlin	37.24
Frankfort	19.52
Dresden	22.15
Strassburg	2.81

The habitation tax has existed in Montreal for a number of years but not in the form of a tax on the rentals of residences. It is a business tax and applies only to the rentals of buildings

¹ Dr. Gustave Koenig, "Un nouvel impot sur la revenu. Mémoire qui a inspiré le projet du Gouvernement relatif à la reforme de la Contribution personnelle Mobilière." Paris, Guillaumin, 1887. Seligman, "Essays in Taxation," pp. 371-372.

² Seligman, "Essays in Taxation," p. 336.

used for business purposes. The tax is levied at a flat rate of $7\frac{1}{2}$ per cent on the rentals of all business property which exceed \$30 a year. There is no personalty or income tax in Montreal, the entire revenue of the city being raised by the tax on real property and on business rentals with the exception of a few special taxes on banks, insurance companies and financial institutions, and the licenses of horses, dogs, peddlers, woodyards, etc. In 1906 the proportion of the total revenue contributed by the business tax on rentals was \$390,548, — approximately 9 per cent.¹ The officials look upon the tax with favor.

The tax on rentals has been in force in Tasmania for some time. There it is not assessed directly on the rental, but on a sum called the taxable amount, and this sum is determined by multiplying the annual value by various numbers ranging from two and one half to ten. The size of the rental determines the number to be used in the multiplication. There are three methods of computing the taxable amount according as the property is used for the following purposes:

First, Residential, or partly residential and partly professional.

Second, Partly residential and partly business.

Third, Lodging.

The taxable amount is highest for the first class, those who occupy buildings as residences wholly, or partly as residences and partly for professional purposes; it is lowest for the second class, those who live in the same building where their business is carried on.

To get the taxable amount for persons in the first class, rentals under £30 are multiplied by five. As the rental increases, larger multipliers are used. Rentals of £1000 and over are multiplied by ten. Similar methods are employed to ascertain the taxable amount in the other two classes, only smaller multipliers are used. The taxable amount thus obtained represents a certain graduation. The tax is then levied at a progressive rate on the taxable amount. The following schedule gives an idea of the progression:²

¹ Report of the Auditor of Montreal, 1906, pp. 112, 113.

² Tasmania, 4 Edward VII, 1904, Ch. 17, Part II.

When the taxable amount is	The tax is 2s. 6d.
under £ 60	
£ 60 and under £ 100	One penny in the pound
£ 100 and under £ 115	2d. in the pound
£ 115 and under £ 150	3d. in the pound
£ 150 and under £ 400	4d. in the pound
£ 400 and over	4d. in the pound for the first £ 400 and 6d. for every pound in excess of first 400 pounds.

A deduction of £30 sterling is made from the taxable amount before levying the tax in cases where the taxable amount is £60 or over, and a further reduction of £10 for each child under seventeen years of age residing with and dependent upon the taxpayer when the taxable amount is under £100, provided such further reduction is claimed by the taxpayer within thirty days of the time when the tax is payable. This provision is an attempt to prevent the tax from bearing unjustly upon persons with larger families.

The tax on rentals was recommended to the legislature as a substitute for the general tax on personalty by the New York Tax Commission of 1871. That commission recommended it as a "Building occupancy tax" to be levied as an additional assessment on a sum equal to three times the annual rent or rental value of all the buildings on the land.¹

In the supplementary report of Professor R. T. Ely of the Report of the Maryland Tax Commission of 1888, a tax on the rental values of places of business was proposed as a substitute for the general tax on personal property.²

In 1897 the Massachusetts Tax Commission recommended that this tax and the tax on inheritances be substituted for the tax on intangible personal property. The recommendation is supported by several pages of argument.

According to this scheme, the minimum rental to be exempt from taxation was fixed at \$400 a year. All rentals of \$400 and over were to be taxed at 10 per cent on the excess of \$400. In every case the sum of \$400 was to be subtracted from the total amount of rent paid. Thus, a person occupying a house

¹ Report New York Tax Commission, 1871, p. 107.

² Report of Maryland Tax Commission, 1888.

whose rental value was \$500 a year would pay a tax of \$10, this being 10 per cent of the excess of rental over \$400. When the rent was \$600, the tax would be \$20; when the rent was \$800, the tax would be \$40; \$1200, \$80, and so on. This tax, as proposed by the commission, was to be levied upon the occupier of a dwelling and of a dwelling only. Houses or parts of houses that were used for business purposes were in no way to be affected by the tax. It was felt by the commission that houses used in business are sufficiently reached by the tax on real property and by the corporation taxes, so that the attempt to tax them again would expose the taxing authorities to the charge of double taxation, and also cause an undue resistance to the new legislation recommended.¹

The latest recommendation is that of the minority of the New York Tax Commission, who in 1906 recommended the tax on rentals as a substitute for the general tax on personalty in that State, and devoted considerable space to setting forth their plan which has been explained above. It is clear that the tax on rentals is in line with the trend of the best thought concerning a rational system of taxation.

¹ Report of Massachusetts Tax Commission, 1897, p. 207.

In rejecting the Report of the Massachusetts Tax Commission, the house committee of the general court said:

"The proposed habitation tax cannot, on the whole, be commended as based on a reasonably good criterion of a man's income, because so many other things than a man's income determine the house he lives in. . . . Even with an earnest desire to avoid hypercritical objections to the carefully thought out schemes proposed in the commissioners' report, any one who stops and for a moment considers the neighbors in his own street or block will see at once how poor a test the rental value of the different houses is of the comparative wealth of the occupiers. The professional man with a large family will often be found occupying as good a house as the childless millionaire. As a single test, the house rental scheme would inevitably prove not only misleading but often oppressive; and the conclusions based upon it would not be nearly so accurate as those arrived at by the average assessor under the present system, which takes into account not only the house but the whole scale of living of the taxpayer, as well as his reputed resources." Report of the Industrial Commission, Vol. 19, p. 1052.

THE UTAH MORTGAGE TAX

BY PROFESSOR GEORGE CORAY

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PREVIOUS to 1892 the laws of Utah provided for a tax on moneys, stocks, bonds, mortgages and similar paper. Up to that time the propriety of such a tax had not been discussed. The small amount of credit business that had been done in the Territory was generally of so simple and unimportant a type, attention had not been called to the peculiarities of security values. In 1891 the Territory, especially in the more populous towns, experienced a boom in real estate, which was of course accompanied by a contagion of money borrowing and reckless indebtedness. It was said of the city of Provo, which then ranked as third in the Territory with respect to population, that after the collapse of the boom in 1893 the people might have profitably moved in a body to another town site, and handed the town of Provo over to its creditors.

Under the old laws, as before stated, these securities were taxable when the transaction happened to be straightforward. What proportion of the revenue to which the Territory was entitled from this source was actually collected can only be surmised. It is significant that when the legislature of 1892 was appealed to by the loan agents and dealers in real estate, no great difficulty was experienced in securing the passage of a law exempting from taxation notes which were secured.

To the man who had never paid a double tax on his home through a medium of a mortgage contract this law looked like an abomination. It was to him, as expressed in one of the chief speeches on this subject in the Constitutional Convention, "the first onslaught of the money interest to free themselves from the burden of taxation." The slogan of the campaign following was, therefore, "Down with the party that had conspired to rob the people for the benefit of money lenders."

The contest was thus forced into the legislature of 1894. But the brokers held their ground and it was passed on to the Constitutional Convention. The chairman of the Committee on Revenue and Taxation had fought with the mortgage taxers in the previous legislature, but he had gained wisdom, as he afterwards explained, and after a long and bitter fight in the committee, an article was reported which provided that in case a mortgage was taxed the amount of the mortgage should be deducted from the property.

This was manifestly intended for a compromise, but it was not sufficient. The debate that followed was bitter and personal. Parliamentary form was quite inadequate to veil the intimation of something worse than errors of judgment.

Scanned under certain well-established rules of economic theory, the debate on both sides betrayed a serious want of systematic knowledge of fundamentals. But no more so perhaps than is manifest in all similar bodies. A summary of the arguments of the advocates of the mortgage tax reveals three distinct points of view. The first concerned itself with revenue pure and simple. Whether the mortgage was substantial wealth or not, whether to tax the mortgage was a species of double taxation or not, whether double taxation was unjust or not, the mortgage was a source of wealth; it was a business factor; it enjoyed and required the protection of the State; it was a regular beneficiary of the governing business to as great an extent and at as great an expense to the people relatively as was any other property, and should not be exempted from the burden of taxation. The advent of statehood would greatly increase the expense of government. The commonwealth was not rich compared with the responsibility it was to assume. It would be a short-sighted and foolish policy thus to relinquish a legitimate source of income by constitutional provision. And this position should be maintained independently of the action of any other State upon the subject of taxation. To take an extreme case: Suppose a person living in Utah to hold stocks of a corporation whose property was in Idaho and, therefore, taxed in Idaho; also, to hold a mortgage on the same corporation. Though the property of the corporation were taxed in another State, both the mortgage

and the stock of the Utah resident should be taxed in Utah for their market value.

"I do not think," says one of the legal combatants, "that this State need concern itself with the tax laws of other sovereignties." For example: "In Ohio they have public officers appointed whose duty it is to investigate the records of other States and Territories with a view to ascertaining the investment made by the citizens of Ohio in those States and Territories, so that they may be brought within the operation of the taxing law." . . . "A man in Ohio goes out to Colorado or Utah and puts his money in a mortgage or real estate; if he does not give it to the tax officer there (in Ohio), and if it shall be discovered by the officer appointed for that purpose by the State, he is retaxed for years with penalties."

The second view presented was that mortgages were wealth, coming as completely under the definition as did any other form of value, and it was a discrimination to exempt them from taxation.

The third view was that the moneyed class was seeking systematically to escape legitimate burdens and should be curtailed by every means within the power of the State.

The position of the opponents to the mortgage tax, as voiced by the chairman of the committee, was, first, that the policy of the State in securing revenue should be to give its attention strictly to property and not to persons, either as individuals or classes. Wherever wealth could be found, it should be taxed once and only once. To tax the same values twice would result in a discrimination against one form or aggregate of capital and in favor of another. And would create an unjust advantage in favor of the person or property exempted.

Now mortgages, stocks and similar securities, as he regarded them, were not wealth in themselves, but the representations of wealth. If they were wealth, they would have a value in themselves and the owner could use that value independently of the substantial property for which they stood. But as a matter of fact he can do nothing of this sort.

Again it is urged that the mortgage, though not the substance of wealth, is the medium through which the possessor is enabled to enjoy the products of industry and government. If that

is so, it must be the industry of the giver of the mortgage which he enjoys. The wealth from this source which the mortgagee enjoys, the mortgagor is deprived of, and he should be relieved from the tax accordingly.

This is what the committee's report provided for, and it was objected to on the ground that the State would thus be depriving itself of a source of revenue.

The chairman's reply to this was, that in so far as the mortgage tax could be collected it would fall ultimately upon the giver and not the holder of the mortgage. The power of the lender of money to exact from the borrower conditions to this end has been proven beyond possible dispute; and this implies double taxation in the most unjust form.

But, as the opponents of the tax contended, any attempt to collect such a tax would result in evasions which would reduce the revenue from that source to a negligible quantity, which would indeed not only deprive the State of its anticipated income, but would inject into the business system of the people of the State methods that are demoralizing far beyond the importance of the face value of the tax, were it collectible.

Another view of the question was, that while the evasions would reduce the revenue to a minimum, there would still remain a resistance to money exchanges which would have to be paid by the borrower; moreover, that some of the home capitalists, rather than resort to dishonorable methods, would send their money out of the State for investment; others would move their residence beyond the state lines while investing their money here, thereby securing an advantage over the local capitalists. It was readily conceded, however, that Ohio was not to be included in these residential attractions beyond the state lines.

In the final action the committee was overruled and the article was finally adopted in the following form, in so far as affects mortgages:

"All property in the State not exempt under the laws of the United States, or under this Constitution, shall be taxed in proportion to its value, to be ascertained as provided by law. The word 'property,' as used in this article, is hereby declared to include moneys, credits, bonds, stocks, franchises and all

matters and things (real, personal and mixed) capable of private ownership; but this shall not be so construed as to authorize the taxation of the stocks of any company or corporation when the property of such company or corporation represented by such stocks has been taxed."

The section providing for the reduction of the tax on mortgaged property, where the mortgage was taxed, was stricken out. In the section on exemptions it was provided, however, that the legislature might authorize a reduction of debts from credits.

Due measures were taken to put the law into effect, and for a time the State realized a snug revenue from the recorded mortgages. But human nature, as outlined by the opponent of the tax, at once began to adjust itself to the new conditions on the lines of greatest advantage and least resistance. As was predicted, devices many were soon available for dodging the law. It was only a question of practice as to which was the most desirable. It is sufficient to say that it took less than a decade to convince those who were watching the developments that the tax was a nuisance. In 1904 the legislature was once more appealed to and in response a measure was passed which provided for submitting to the people a constitutional amendment to prohibit the taxing of mortgages.

The grounds for the reaction were, that in so far as the tax was collected it was paid by the holder of the mortgaged property, and thus burdened him with a double tax; that it tended to raise interest; that the tax applied only to residents of Utah and placed them at a disadvantage with foreign competitors; that as a result of this disadvantage dishonorable devices were resorted to in the loaning of local money.

The device which did most of the work was, to loan the money in the name of a non-resident friend and to take from him a perpetual power of attorney with respect to the mortgage. Another way was to receive from the mortgagor a deed for the premises and then to place a quit claim in escrow to be delivered upon payment of the note.

A third device was for local people to organize a corporation under the laws of another State and make out their mortgages in the name of the alleged foreign corporation.

Some of the wealthy residents who had been in the habit of loaning their money in Utah found that they could move their residence and live in a measure of luxury on the money they would otherwise have had to pay out on mortgage taxes. Some money went out of the State for investment, but the amount seems to have been unimportant.

As an example of the character of the loaning business under the taxing system, it is reported that among those who employed the foreign residence device was an ex-judge of the supreme bench of the State, who for years loaned upwards of \$30,000 in the name of a relative residing not far from Ohio — but far enough to escape taxation.

In 1906 the amendment was submitted to the people and passed, and by no means were all who voted for it unaware of the injustice it carried.

GOVERNOR DAWSON: Gentlemen, this concludes the regular program for the morning, and the next thing in order is the discussion of the papers and addresses submitted. I am requested to say a word about the discussion and to gently hint to the delegates that it does not consist solely in asking questions of the authors and speakers, because it may be that they have told you all they know and it might be embarrassing to probe further in that direction. Besides that, we want the discussions and the opinions of other people. Now we are ready to hear discussion.

MR. POTTLE (Maine): I had an opportunity yesterday to examine hastily the paper which was read by the gentleman from North Dakota, Professor Boyle, and I bespeak for it, when it shall be published in the proceedings of this convention, a most careful and thorough examination, as a record, though quite a brief one, of the facts in connection with a subject of taxation in which we are deeply interested. The subject of taxation is too broad to be treated briefly, and I think the authors of the several papers read here have done excellent work, considering the very few minutes they are allowed to speak under the rules of this meeting.

The question of taxation has vexed the minds of men since the earliest days of history and of civilized government, and the last word has not yet been said. The last word will not be said here. As stated by the distinguished gentleman from Iowa, the last chapter in our experience has not yet been written. I am glad to see here men who have borne the burden and the heat of the day, the earnest men who have been for years in practical touch with this question of taxation. I am glad to see here also young men, men who represent the newer thought, the latest thought, and I believe that from this Conference will flow results, perhaps not at once perceptible, but ultimate results, that will work a new era in taxation in the several States of this Union. I congratulate you all upon the sessions of this Conference thus far, and for myself, coming

as I have nearly a thousand miles from the State of the rising sun, I feel already well paid for the journey here.

MR. THOMAS (Utah): I want to refer to one or two matters in the paper of Professor Boyle. He stated that those States whose boards of equalization provided that terminals of railroads should be assessed for more than other parts of the railroads running through the State, were wrong; and that those States which provided that the corporation or its trackage should be assessed as a whole, should be apportioned to the trackage of the various counties in the State, were correct. Now, it seems to me that the remarks of Mr. Purdy yesterday were correct and appropriate. He stated that the question of taxation was one of history and environment, and I think that is a true statement. Take my own State: we have railroads running through its length and breadth; in some counties they go through deserts, in other parts, through irrigated, fertile valleys. I have in mind one county that has seventy-nine miles of railroad; in that county there are about eleven hundred people; that county is about seventy-nine miles long and sixty miles wide. They have but two school districts. The assessed valuation is about \$1,400,000, of which the railroad pays on a valuation of over \$1,100,000. Now, if that tax were apportioned to the trackage throughout the State, this county, that has now no means of expending the revenue which it receives, except to keep on building new schoolhouses, would receive more than it needs, and other parts of the State, where the burden falls most heavily, would not receive their proper proportion. In the city of Salt Lake, one of the largest trans-continental railroads has over sixty miles of sidetracks upon land that you could not buy probably for \$1,500,000. The great burden of taxation of the State comes upon Salt Lake County, and if that terminal doctrine were in its book of laws, one part of the State would bear the whole burden. I simply make this statement, for the reason that I think, in the published paper of the gentleman, he should modify his statement. As Mr. Purdy said, it is a question of the environment and the history of the State.

There is another matter to which I wish to refer, that was a statement upon the question of the assessment of live stock in

Wyoming. Wyoming is a neighbor State, and I am familiar with the conditions there and its questions of taxation. Wyoming is an agricultural State, I should say, perhaps, a stock-raising State. The total valuation of Wyoming is scarcely \$50,000,000, which is simply a drop in the bucket in comparison with your Eastern States. I think I should mention these facts in justice to Wyoming, because they also apply to my own State. We have one county in our State, the largest county in it, casting about a hundred and fifty votes, where they are assessed nearly a million dollars. These things occur to me, and perhaps the gentleman may wish to consider them before his paper is published.

Ex-GOVERNOR WHITE (West Virginia): There was another statement in the paper to which the gentleman from Utah has just referred, with which I would like to take issue. It was not my privilege to hear Mr. Purdy's address. I console myself with the fact that I shall be permitted to read it in the published proceedings; but I gathered from the gentleman who spoke this morning that Mr. Purdy took the sound, sensible stand, from my viewpoint, that railroads should be assessed, as all other property, annually. The gentleman who read the paper this morning volunteered the suggestion or statement that he thought once in five years was often enough to assess railroads. I presume the railroads in his State are assessed as real estate on the property book. I take it that he does not mean that he wants to assess the railroads only once in five years. I believe, if he thinks a little more deeply along that line, if his State is ever favored with an oil development, or a natural gas development, or with a rapid municipal development, he will find that five years is a period in which tremendous fluctuations in values may occur. Now, in my own State we used to have the absurd Ohio idea of assessing about once in every ten years, and if there ever was a system born of imbecility, it was that system of assessing real estate only once in ten years. That is one of the reasons, Mr. Chairman, why I have rarely alluded to the fact that I was born in Ohio, and that I left it so many years ago. It is the crudest and most absurd system of assessing property ever practiced by any State in the Union.

What I am endeavoring to say to my friends and to urge, in this semi-humorous way — for I have been a taxpayer in Ohio for a great many years — is, that the assessment of real estate, if it is worth anything in a growing, developing community, should be just the same as that of personal property, or railroads, or any other assessment of value — annual, so that the equilibrium of value may be maintained. In our own State, a tremendous oil and gas development may arise and disappear in five years. Our railroads are building through great lumber districts, and the lumber or timber may disappear before the increased value added to it by the great facilities of transportation can go into the tax duplicate. I simply want to impress upon you my view as to the annual assessment of all property, as being the correct idea.

One other observation. We have had some problems in our State, and I do not think any other State in the Union in three years made such a revolution — complete and absolute revolution in tax matters — as the State of West Virginia. I see no papers here and have thus far heard nothing in the addresses or discussions as to the limitations of the tax levy. We are all talking about assessing property and getting it into the tax duplicate; but when we are talking about that, we are talking from the special interest side, the side of the railroads, which are always watching the assessments; and we lose sight of another side, that is, gentlemen, when you arrive at a fair system of taxation, how will you hold the rate down to something reasonable and proper? The limitation of the tax levy is an important part of the problem of taxation, an important phase of the assessment of property. To illustrate: In our State, we have adopted the only standard of measurement which I think is rational, that is, the true and actual value of property, further defined in the statute as the value which that property would bring when sold at private sale, under usual conditions, normal conditions of trade and business — the true and actual value of the property. We have heard that in one State they take 20 per cent of the value. One gentleman, I believe, referred to Minnesota, which had raised the value of municipal lands and then taken 40 per cent of their value, and I judge from that remark that 40 per cent was taken

to be about the average yardstick of measurement for their real estate values in that State. The true and actual value put on the tax duplicate would mean in the State of Ohio multiplying every tax duplicate possibly by the figures three and one half or four. Now, if you adopt the rational value, you would have to safeguard the taxpayer. That is a problem we have in West Virginia. When we adopted that standard, we increased the taxable value of all property in that State from \$287,000,000 to over \$900,000,000, an increase of three times and more the amount. I want to say, as a citizen of that State, that the average tax rate for all purposes, schools, districts — that corresponds to townships in Ohio — municipal, county, State and everything, for the State of West Virginia last year was sixty-seven thousandths of 1 per cent; that was the average rate of taxation for all purposes. Compare that with the towns or townships in the State of Ohio, or in the places where they take 40 per cent of the value, or in Illinois with its 20 per cent. I was interested in the answer the gentleman gave last night to the question why they take 20 per cent in Illinois; he put it upon the ground that certain interests in Chicago objected to paying more than their proportion. The real fact is, large taxpayers will not submit to the full, actual value as the yardstick of measurement, unless the rate of levy is safeguarded at the same time. Now, in our own State, to make it short, our tax levies run something as they do in this State; some counties $3\frac{1}{2}$ per cent. Now, we limited the tax levy and we limited the amount they can levy, and the present limit for county purposes is thirty-five cents on the hundred dollars, that is thirty-five hundredths of 1 per cent. The State tax when the law was adopted was thirty-five cents on the hundred dollars; this year it is five cents on the hundred dollars. The municipal taxes were limited to forty cents on the hundred dollars; that is, forty hundredths of 1 per cent. The school levies are limited, but there are certain exceptions; I will mention the city of Wheeling, the leading city in the State: her total taxes this fall for all purposes, school, State and district, county also, are eighty-eight and one half cents on the hundred dollars, or eighty-eight hundredths of 1 per cent, and we propose to still further limit it, and to put into statute,

if we can get the views of the legislature to coincide with ours, that the taxes for all purposes in one municipality shall not exceed 1 per cent, or one dollar on the hundred, and if they need any additional taxes for school, county or State purposes, they will have to go to the people for their approval by special vote; in other words, we hope to have the maximum for all property limited absolutely to 1 per cent. There are some three hundred districts or townships in West Virginia, and there are nearly fifty in which the combined taxes for all purposes are one half of 1 per cent, or fifty cents on the hundred dollars, or less; the lowest tax is thirty-nine and one half cents on the hundred dollars. That is the result of true and actual value, backed up with a corresponding levy limitation. I simply want to throw the weight of our experience on the side of the actual assessment of property, if we are going to have a system which levies values with some rational idea of their relation to the taxation of the current year.

MR. ROBINSON (Kentucky): I think the statement we have just heard is one of the most interesting and practical of any we have had. I would like to ask the gentleman one or two questions; I would like to ask if the increase in valuation was altogether in the increased value of real property?

EX-GOVERNOR WHITE (West Virginia): The personal property increases have not been in proportion to the realty. The railroads, public service corporations, are raised under the present Governor from about forty millions to about a hundred and ninety millions,—over four times. The personal property problem is still a problem with us; but as we get the limitation on the levy down, we hope to get the personal property valuation up.

MR. ROBINSON (Kentucky): I will ask as to whether your rate on personalty throughout is the same as the rate on realty?

EX-GOVERNOR WHITE (West Virginia): Necessarily so, from our constitutional limitation, which is the only excuse for its being so; all property, no matter what it is, has to be measured by the same yardstick.

MR. CRANDON (Illinois): I want to give my opinion in favor of the actual assessment of realty, and property generally, in

agreement with the opinion just expressed. I want to ascertain, if I can, what is the special advantage of assessing property at full value and making a tax of 1 per cent, over the assessing of the same property for taxable purposes at one fifth of the value and permitting it to be taxed at 5 per cent? The results are precisely the same. In Illinois we assess property at 20 per cent of its value.

EX-GOVERNOR WHITE (West Virginia): Do you assess money at 20 per cent of its value?

MR. CRANDON (Illinois): As a matter of fact, no; but as a matter of law, yes.

EX-GOVERNOR WHITE (West Virginia): You mean as a matter of law, no, and as a matter of fact, yes, do you not? That is, the law permits you to take 20 per cent, if you will.

MR. CRANDON (Illinois): Twenty per cent of everything, sir, whether it is money, live stock or real estate, household goods, or any other property; it is all assessed at 20 per cent of its true value — 20 per cent of its value. I cannot see how the taxpayer is going to be helped particularly by having his property assessed at full value and paying on that 1 per cent, over the plan of being assessed at one fifth of its value and paying 5 per cent; and I do not see why we should go to West Virginia and adopt its plan unless some better reason for doing so can be given than has already been presented.

EX-GOVERNOR WHITE (West Virginia): West Virginia hasn't a patent on it; it is just common sense, that's all.

MR. CRANDON (Illinois): Common sense, why? Is one fifth of the real value at 5 per cent a less sensible thing than the full value at 1 per cent?

A DELEGATE: But in order to assess the 20 per cent of the full value, would you not first have to find the real, or the full value of the property?

MR. CRANDON (Illinois): Where is the gentleman from?

A DELEGATE: Missouri. (*Laughter.*)

MR. CRANDON (Illinois): I want to refer to one other feature if I may, while I am on my feet. The paper read by the gentleman from Minnesota this morning spoke with very great appreciation of the tax commission of that State. I think well of the tax commissions about which I know and I have

some familiarity with several of them, in Michigan, in Wisconsin and in Minnesota, and I find also, that the one thing or the one feature which he presented is especially the thing to be commended in a tax commission. The one thing for which he praised the tax commission of Minnesota was, that it was increasing the assessment of iron land from a small sum to a large one. Well, if it ought to be so increased, yes. But is it the business of a tax commission simply to increase the assessment of one class of property? Is that the only thing that the tax commission is to do? If the land, if personal property and if mixed property throughout the State is assessed at 40 per cent of its value, is the commission to be lauded because it has unduly raised the assessment on iron lands? I do not know anything about what value those iron lands have, but in Illinois the constitution says that taxes shall be levied in pursuance of assessments so that every person pays a tax according to his, her or its property, and that should always be the aim of all taxing bodies, not particularly that you raise one class of property to a high valuation, leaving others to pay on a low proportional value, but that equilibrium shall exist in the assessment for taxation of all property.

MR. PHELAN (Minnesota): I would like to say that I referred to the increase of valuation of iron land as an attempt upon the part of the tax commission to equalize taxes on each kind of property. I think I stated that the 40 per cent valuation placed upon this property is believed to be the general rate upon property throughout the State. The iron mines were raised in valuation to bring them up on a level with other kinds of property.

EX-GOVERNOR WHITE (West Virginia): Not a statute rate?

MR. PHELAN (Minnesota): No.

MR. DUBUQUE (Massachusetts): One of the speakers referred to the very interesting and important question of situs. That is, of course, very important as bearing upon the question of getting foreign capital into any State needing development. One great trouble has been the refusal of the United States Supreme Court to interfere with the tax laws of the States. Now, it seems clear, from a great many decisions of the Supreme Court, that credits can have but one situs. In the case of a state

tax upon foreign held bonds, it was held that the situs was with the owner of the credits; then in the *Western* case it was said that there was a situs in the part of real estate which was mortgaged, or, in other words, in the mortgagee's interest in real estate, and that the State might tax that interest which the mortgagee had in real estate, just as it might tax a mortgagor's interest. It was also said, however, that the right of taxation did not exist unless the State passed a law to tax it. In the State of Kentucky it is held that the laws do not tax such an interest; consequently, money which is loaned by foreign bondholders, although secured by mortgage in Kentucky, is not taxable in Kentucky. The Supreme Court has passed upon a number of cases, one, a case from Louisiana, where the Supreme Court held that property, although in the shape of bonds, or even a promissory note, being within the State, had a situs within the State. In the case of *Burke vs. Beach*, a man in New York had loaned money in Ohio upon mortgages in Ohio, and his notes, secured by mortgage, were sent to La Fayette, Ind., and were there in a safe with his own agent. Those notes were, whenever assessment day came around in Indiana, sent to Ohio, and the question arose as to whether they had a situs in the State of Indiana. The Supreme Court of the United States held that they had no situs within the State of Indiana and could not be taxed within the State. The Court also indicated that the view which it took would tend to discourage double taxation, but it did not say that double taxation was inadmissible. Now, it would seem to me that if the question were finally pressed upon the Supreme Court that it must say that such property could not be taxed twice, or in other words, that the property could not have situs in two places, it must have a situs in one State, and if it has situs in one State, it could not be taxed in another State. It seems to me the Supreme Court have said that. If that be true, how can there be more than one situs to property? And if there be one situs, then but one State can tax it. If you cannot tax real estate outside of the State of taxation, then you cannot tax personal property outside of it. It is now decided by the Supreme Court that personal property is wherever the evidences of it exist, so far as negotiable instruments

are concerned, and that the trouble is solely with those things that are intangible. If it exists simply in contemplation, if a debt which is secured by no instrument, there can no situs exist. Now, it seems to me that if the question be finally pressed upon the Supreme Court, it must determine that a thing can have but one situs, that it can exist in only one place, and only the State where it exists can tax it. So that if there be anybody here who may have such a case and will finally bring it before the Supreme Court, and if the Supreme Court cannot be brought to a realization of the necessity of finally settling the question, then certainly the States may consider the case of *Burke vs. Beach*, and may frame their laws on the ground of interstate comity to meet it.

A DELEGATE: I want to ask you this question: what you would do with cars belonging to car companies, like the Armour cars?

MR. DUBUQUE: Those cars are generally assessed upon a mileage basis. Where they go into different States, they are supposed to have a situs in all of them and be distributed according to a mileage basis. This was held in the telegraph and express cases in the 165th and 166th United States. Of course, the Supreme Court there did not mean that one State might tax the franchise of a telegraph or express company in another State, but simply that there must be some way to distribute the values between the different States, and that one practicable way was to take the mileage basis. Another way was to take the basis of earnings; but at last the theory was that you were assessing solely what was within the State. Every other State adopting the same method would arrive at the same result.

A DELEGATE: You have now made clear what I thought you meant—that you did not mean a fixed situs, but a shifting situs. The situs would depend upon the character of the property.

MR. DUBUQUE: Yes, whether you tax the thing itself or the chose in action.

A DELEGATE: Well, it is very difficult to lay down any hard and fast rule in taxation.

MR. DUBUQUE: Unless the Supreme Court will announce a ruling.

FOURTH SESSION

WEDNESDAY AFTERNOON, NOVEMBER 13, 1907, 2 TO 5 O'CLOCK

CHAIRMEN: MR. LAWSON PURDY OF NEW YORK,
GOVERNOR GUILD OF MASSACHUSETTS

PROGRAM

1. THE RELATION OF FEDERAL TO STATE AND LOCAL TAXATION.
Professor H. Parker Willis, Professor of Finance, George Washington University; Washington Correspondent *New York Journal of Commerce*, Washington, D.C.
2. TAXATION OF INHERITANCES.
Professor Joseph H. Underwood, Professor of Economics, University of Montana, Missoula, Mont.
3. TAXATION OF INHERITANCES.
Dr. Max West, Bureau of Corporations, Washington, D.C.
4. THE POSITION OF THE INHERITANCE TAX IN THE AMERICAN SYSTEM OF TAXATION.
Professor Charles J. Bullock, Department of Economics, Harvard University, Cambridge, Mass.
5. TAXATION OF INCOMES.
Professor Charles Lee Raper, Professor of Political Economy, University of North Carolina, Chapel Hill, N.C.
6. TAXATION OF THE PRODUCTS OF AGRICULTURE.
N. J. Bachelder, Master National Grange, Concord, N.H.
7. FOREST TAXATION.
A. C. Shaw, Principal Examiner Law Office, U. S. Forest Service, Washington, D.C.
8. DISCUSSION.

THE RELATION OF FEDERAL TO STATE AND LOCAL TAXATION

BY H. PARKER WILLIS

Professor of Finance, George Washington University; Washington
Correspondent *New York Journal of Commerce*, Washington, D.C.

IN any study of fiscal and revenue problems it is well to bear in mind, first of all, the exigencies of practical legislation and legislative relationships. Financial needs must be met from day to day; and, if not to be logically answered, will be dealt with from the standpoint of expediency. This is one reason why it is conspicuously necessary to consider such problems from a somewhat opportunistic point of view, and to bear in mind that improvement and reform will be a slow growth, proceeding by some process of accretion and substitution rather than by complete transformation. In what is here set forth, therefore, it will be assumed that the problem is dealt with under practical conditions, subject to existing constitutional restrictions and in no way on an ideal or abstract basis.

The choice of federal sources of taxation, as at present made, has been the result of constitutional provision in part, and of experience in part. Like the States and municipalities, the federal government has gone on in developing its fiscal system without regard to other units of government. It has been guided solely by its own experience as to cheapness and expediency in collecting revenue; and it originally settled down not unnaturally upon those fields of taxation in which it has sole and undisputed authority. The exaction of customs duties was soon found to be both the cheapest, the least annoying and conspicuous, and the most unquestionably constitutional way of raising revenue. The excise system followed closely on the heels of the tariff, historically. It was an adaptation from European experience and was justified by the courts by the usual ingenious interpretation of the Constitution. How

greatly its extension would possibly result in revenue, and how widely it could theoretically be broadened, are obvious considerations already exemplified in various national crises and requiring no further illustration.

Experience, however, in this case as in that of the tariff, has marked out with great clearness the lines of least resistance along which the government can move with safety in imposing such taxes. As a result of such experience we now have a national revenue which in the fiscal year 1907 aggregated \$663,140,000 exclusive of postal receipts. Of this sum \$332,233,000 came from customs and \$269,666,000 from "internal revenue," or in plain language came largely from the taxes upon the consumption of liquors, beer and tobacco, the relatively small balance being derived from sales of public lands and miscellaneous items. It is probable that the drift thus indicated will be maintained, and, in the main, there is no reason to demand that a different course be pursued. With matters as they are industrially, a national revenue depending first of all upon the two sources of revenue already referred to, will be unavoidable. It does not necessarily imply an adherence either to protective or tariff for revenue policies since the amount of revenue ultimately yielded by tariffs is often more or less independent of the protective or revenue purpose originally contemplated by given duties. At all events, the continuance of such a fundamental federal revenue system must be taken as the first assumption in the study of national taxation in its relation to the revenue systems of the smaller units of administration and government.

But there are at present serious dangers threatening a plan of exclusive dependence on customs and excises like that which is here suggested. The rising expenses of the federal government indicate that the funds from tariff and internal duties, hitherto in the main amply sufficient for all current needs and even sufficing at times to bring about large reductions of the national debt, will, in the comparatively near future, be inadequate to meet these requirements. This thought is forced upon the attention by the fact that from two sources tendencies are now pressing the nation in the direction of a change in national fiscal conditions. It is apparent that some very large enterprises of a semi-economic nature are to be undertaken. One feature

of such a movement is already seen in the construction of the Panama Canal — an undertaking which, it is true, is largely to be borne by the issue of bonds, but which must ultimately be paid for, and can probably be liquidated, only through the imposition of fresh burdens either now or in the future upon the tax contributors of the United States. Further, the extensive scheme of internal waterway improvement which is being demanded by the cities and States of the Middle West, and which has been endorsed by the President, will undoubtedly continue to demand attention until, at some time not far off, it is met by the expenditure of very large sums of money — sums which, according to current plans, may far surpass those required in the construction of the Panama Canal. The upbuilding of a strong navy is an idea which seems to have the support of a majority of the people (so far as the average man devotes any thought whatever to the subject) while proper coast fortification and the corresponding enlargement of the army will require increasing outlays. What we shall have to do in our Oriental dependencies and how much outlay will there be needed, is another question requiring the most serious thought. This is not a discussion of the tendencies of federal expenditure, and further reflection on the probable lines of future outlay must be referred to some more appropriate place. Enough has, however, been said to indicate the point which it is desired here to emphasize — that in the future there will be a call for the expenditure of federal funds in amounts for which the present revenue sources of the country will probably prove inadequate. On the other hand, it is to be noted that the opposition to excessive rates of duty and the desire for reciprocity arrangements with foreign countries is evidently on the increase. This necessarily signifies that tariff revision will imply some reduction of duties, and it is not an unreasonable prediction to say that it may be no very great period before the tariff will be materially altered and the revenue from it in some measure reduced. There has been no falling off in incomes from internal taxes, but rather in the recent past they have shown a strong upward tendency such as to make it apparent that there is here a continuing source of revenue. Yet it is obvious also that the strength of the movement against the sale of liquors, which has already cut off a percentage of the in-

come derived from this source in some of the Southern States, may yet impair one side of the revenue and may cut it in the future to a point much below that which it has now reached. The readjustment of rates of duty on alcoholic beverages would doubtless make the taxes more productive than they are at present, and this is likely to be undertaken at a date in the near future. Enough, however, has been said to indicate the probability that there will be need of additional taxes on which to draw for income in the not distant future.

Along with powerful tendencies to increased federal expenditure and with the possibility of a considerable falling off in income must be considered another class of considerations affecting this matter. This is found in the fact that a strong movement is in progress having for its object to bring about the regulation of wealth and of social conditions through the imposition of federal taxation. The alleged menace of "swollen fortunes," — the desire to control industry through federal taxation, the effort to rectify economic evils of many kinds by national rather than by individual means, — all point to the probability that either a vigorous executive, or a Congress driven to the wall and compelled to provide means for unforeseen necessities, will afford an impetus leading to the adoption of new sources of taxation by the federal government. That these will be so chosen as to throw into further confusion the already distorted fiscal systems of the several States is a danger which must be provided against.

Experience shows that this danger is far from imaginary. The confused and disastrous fiscal legislation of the Civil War, the illogical extension of the internal revenue system to include many disconnected and unrelated objects of taxation, the hasty and ill-advised expedients resorted to more recently under the anticipated stress of the Spanish War, all show to what lengths the federal government is capable of going when an adequate impulse is afforded and how ill-chosen are the means which it adopts upon occasion. It would be highly undesirable to have the helter-skelter systems of taxation heretofore accepted in time of necessity as a temporary expedient resorted to as a permanency and perpetuated in permanent form. Were this situation to come into existence, it would imply something more

than merely the establishment of an unfair and unwise plan of raising federal revenues. It would mean that the state and local systems of taxation which have thus far been kept fairly free from national interference, save at crises in national history like those already referred to, would be infringed upon, their natural sources of revenue cut into, and possibilities of double taxation, considerably exceeding those which have existed in the past, brought forward. This danger must be avoided, but it can be guarded against only through the selection of some permanent source of federal taxation, coördinate with the two great sources now in use, which shall be elastic and productive. It must be elastic that the rate may be freely changed with a practical certainty of gathering revenues to cover deficits produced through shortage of tariff and excise incomes. It must be productive in order that no recourse to other sources of income will be necessary under any ordinary stress of necessity.

England has pointed the way in this matter by her policy in reference to the use of the income tax. That tax as now employed affords an expansible and reliable mode of filling up all deficits in the national budget which may arise either owing to deficiency of other revenues, or to large requirements for new national necessities for war or for meeting obligations. If some similar source could be found for the federal government and could be definitely accepted as the mainstay of the Treasury in cases where extraordinary revenues were called for, a long step in advance, from the technical fiscal point of view, would have been taken and the relation of federal taxation to state and local taxes would have been brought much nearer to a satisfactory basis than heretofore. Two general suggestions may be made for the selection of some such source of taxation. One is the familiar income tax idea, the other a tax or group of taxes levied upon interstate commerce. The income tax has been thought of by many persons as a mode of redressing inequalities arising from the reliance placed in our government upon tariffs and excises, and has approached more nearly to enactment into law than any other. It has been tried during the Civil War with some degree of extensiveness. But in the main it must be conceded that the income tax has not been a success. It has developed a difficulty of collection and assessment, an

elusiveness in sources of income growing out of our peculiar constitutional provisions, and a tendency to conflict with the legislation of the States, which seems to indicate that it is less adapted to the peculiar requirements of federal finance than to those of the commonwealths or of the foreign governments which have adopted it. The last consideration is the most important of all for the present purpose. The choice of the income tax as a federal resource of permanent character could be made and might conceivably be successful, but would involve delicate adjustments. It would also contain the constant possibility, even should the courts look kindly upon it in theory, that States would by their adoption or maintenance of similar systems of taxation throw the machinery out of joint. It is in harmony with present federal tendencies, far more likely to avoid difficulties of a legal or quasi legal nature, and far more feasible as an integral part of a well-adjusted system of taxation in the future, to select as the ultimate mainstay of the Treasury a tax upon corporations of all classes engaged in interstate commerce. Interstate commerce is the phase of government to which the Constitution especially addresses itself, and in which it sought to give the federal government most absolute authority. Such a tax can be chosen in a way to attain almost any desired result and to be either a large revenue producer or a restriction upon certain kinds of business. It may operate as a means of controlling corporate capitalization through the medium of a national incorporation act, or as a mode of enforcing the return of proper information from interstate carriers, or as a means of controlling earnings and of taking for the government the excess value of franchises. It can be applied in a way that will lay it open to no charge of unreasonable exaction. It may be levied on a basis that will assure its ultimate payment by those from whom it is first claimed or will suffer it, if desired, to be transferred in part to the shoulders of the general consumer, as is done with the tariff and the excise duties. It will be seen that this suggestion raises many important problems. It calls up the question whether national incorporation laws are desirable, necessary or feasible. In choosing the form of the tax, difficult legal issues will also have to be dealt with if constitutional obstacles like those raised by the Supreme Court in

connection with limitations upon direct taxation are to be avoided. This large topic is, however, a detail in the larger field covered by the present brief discussion and cannot be debated now.

The selection of tariff and excise duties, accompanied by some such third source of taxation as has been suggested, implies some very direct inferences with reference to the choice of state and local taxes. These are too often neglected, but must receive consideration in any reasonable or scientific arrangement of revenue laws from the standpoint of the whole nation. This relationship is dependent primarily upon the question of incidence and must be so considered. Accepting the idea that a distribution of taxation equitably in accordance with faculty is desirable, it is apparent that the taxes chosen as a means of providing revenue for the States and local government must be such as to relieve in largest measure those tax contributors who are called upon for the bulk of the federal support.

In non-political discussions there is usually little disposition to question the general character of the incidence of tariff and excise duties. The bulk of our imported goods are manufactures. Tariff duties are imposed upon them as an incident in their distribution. With some few modifications, it may be said that the duties tend to form a regular feature of their cost of delivery and are in the main exacted of the ultimate consumer. Since, moreover, the collection of tariff duties in amounts to yield considerable revenues is bottomed upon a wide demand for the goods, it is a necessary consequence that the collection takes place over a wide area of buyers. They are, in short, collected in the majority of cases from consumers of small or moderate means and have the general effect of raising the cost of some of the most necessary articles of consumption. So also with the excise taxes upon which the government depends for a large part of its regular revenue. They are collected from a class of persons who, in the main, are but little governed in the strength of their demand for these articles by considerations of price. The elasticity of demand in such cases is nearly constant and the effect of the taxes is to take from the great mass of consumers of the articles upon which they bear an added increment exacted through the medium of a higher price. While it is perfectly true

that the whisky, spirits, beer and tobacco upon which the government now levies its main internal revenue duties are in no arrangement of economic wants to be classed as necessities, it is also true that the consumer often so regards them, or at all events acts as if he did, so that legislation upon fiscal matters must necessarily recognize this condition of affairs and deal with it accordingly. The incidence of some such tax upon interstate commerce, as has been suggested, would conform to the familiar laws of price which govern the distribution of all taxation. On the whole, it is safe to assume that there would tend to be a transfer of far the greater part of such a tax to the shoulders of the general consumer. It may be stated that both now and in the future, the man of small means, the general consumer and the person whose immediate wants require the greater part of his income will have to bear the main load in the support of the federal government. A modification of the tariff would be of service to the bearers of this burden, but it is probable that the loads which they now carry would continue to rest upon them through the imposition of similar taxes differently devised. A better distribution and classification of tariff and excise of burdens would be of large service, but would not change the present general responsibility for the cost of government.

If this view of the incidence of federal taxation be accepted, it is clear that an equitable scheme of state and local taxation will endeavor primarily to draw upon those sources of taxation which are untouched by the operation of federal statutes. In a general way, the implication of this principle is obvious. State and local taxes must be those which will operate as little as possible upon the man of small or moderate means and will draw as largely as possible from those whose resources are more extensive. It is worth while to note the changes that would thus be introduced into present methods of distributing taxes in the different communities. It would imply in municipalities and States an abandonment, so far as possible, of general property taxes and a recourse to those which would fall either upon persons of large means or upon those who were in position to absorb the increments arising from growth in population or from the use of natural opportunities. In cities it would point to a recourse

first of all to taxes upon municipal monopolies and the franchise privileges within the gift of the municipality. These would be taxed in such a way as to extract from them the chief increments of value due to growth in population and to changes in the amount and distribution of wealth. Probably the real estate tax, imposed in such a way as to fall most heavily upon increasing values due to situation, would form an important element in the city's budget, and this, together with the usual proceeds of licenses, special assessments and the like, would afford the sources of necessary income. For the rural communities a properly adjusted land tax, based on carefully ascertained valuations and coupled with such fees and special assessments as were deemed requisite, would supply the limited needs of town and county government. The States would be shut off from the proceeds of the land taxes which they now collect. They would be confined to taxes levied upon inheritances and the higher grades of incomes, upon the corporations they create, or the intra-state business of interstate corporations. Taxes upon natural monopolies wholly situate within a State would contribute their share of revenue. It would be recognized that the individual as an income-earner had performed his duty in supporting the general government and, in the main, the other grades of government would not look to him save in so far as he enjoyed some exceptional privilege or some unusual opportunity afforded him for profiting from the advance of the community in wealth and in population.

In all of these adjustments the problems arising would be largely dependent upon the establishment of proper relationships between the States and the local governments. Avoidance of the domain selected by the federal government would be comparatively easy. The main requisite would be, so far as possible, to relieve the general consumer from further incidence of taxation and to choose for the States and localities those sources which would permit of shifting only in the most minor degree. In short, the proper adjustment of federal to State and local taxation seems, from the present standpoint, to be summed up in the following propositions:

1. Retention of tariff and excise taxation as the mainstay of federal finance.

2. The addition of a third principal source of revenue, such source to be found preferably in a properly adjusted tax upon interstate commerce and the corporations engaged therein. The form of this tax must be determined by a careful study of modes for the adjustment to constitutional principles. Different phases of the tax might be reserved for police or control purposes in cases where the exertion of such economic power was deemed expedient.

3. The limitation of state and municipal taxes, so far as possible, to sources of monopolistic revenue; accompanied, in case of necessity, by income and inheritance taxes with high minimum exemptions.

4. In every case the effort to relieve the general consumer in State and local taxation of contribution to the cost of government, attaining this end by selecting objects of taxation with a view to the smallest possibility of shifting such taxes.

THE TAXATION OF INHERITANCES

BY JOSEPH H. UNDERWOOD

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A DEFENSE of the taxation of inheritances is superfluous. Its existence in all but a few of the civilized nations and in all but a few of the more backward States is its chief defense. It is to be found in Australasia, Austria, Belgium, British Provinces, Canada (Quebec and Ontario), Denmark, England, France, Germany, Greece, Holland, Italy, Portugal, Russia, Spain, Sweden, Switzerland, and in thirty-three States of the Union. The recent utterance of the President of the United States, looking toward limitation of inheritances by taxation and the tendency to extend taxation of this character in amount, makes pertinent a defense of such extension. The President says: "I feel that we shall ultimately have to consider the adoption of some such scheme as that of a progressive tax on all fortunes, beyond a certain amount, either given in life or devised or bequeathed upon death to any individual — a tax so framed as to put it out of the power of the owner of one of these enormous fortunes to hand more than a certain amount to any one individual; the tax, of course, to be imposed by the national and not the state government. Such taxation should, of course, be aimed merely at the inheritance or transmission in their entirety of those fortunes swollen beyond all healthy limits." Rapid increase of such taxation for the purpose of strengthening the supremacy of the State is assumed to conflict with the right of a man to do what he will with his own; but it is not so definitely determined that a man who no longer lives may deal quite so freely with his own, or that a man who has not yet owned may deal quite so freely with what he expects to own. The right of unlimited acquisition may have been generally added to the incidents of property, but it is not certain that expectancy has yet been added to the list of the rights of property.

It is not yet absolutely conceded that a man may confer upon his infant grandsons a potential status in society greater than that he himself had attained.

Although political expediency and social welfare are the principles to which appeal may be chiefly made in support of the "death duty" or the "heriot," the actual reasons for its adoptions and extension in most States is doubtless to be found in the everyday consideration of the attractiveness as a revenue producer. Thus it produces large revenues in New York and Illinois, while in a new State like Washington, where it is well administered, it produces \$50,000 annually. The revenues are still larger in Europe, where this tax is more completely applied, the "death duties" of England reaching to perhaps £20,000,000 yearly. Thus the reason for its adoption in Washington and in South Dakota is stated to be, "to produce revenue." Mere custom has dictated its adoption in some States. Thus the state treasurer of Wyoming gives as a reason, "the custom in many States." The treasurer of Montana says the Montana law was passed, "to raise more revenue and following the laws of other States." Another familiar reason is that stated by the Governor of Oregon,¹ "that many, if not all, estates going through probate have escaped their just share of the burdens of taxation during the lifetime of the decedent." The clerk of the Idaho Supreme Court states the reason of his State, "for revenue primarily, and incidentally as a means of making accumulations of wealth pay a larger share of the burdens of taxation."

The theory that it is a back tax seems to be justified by the opinion of Goschen: "I think it will be found that the men whose fortunes are considerable are those who pay the least in proportion to their aggregate income;"² and by the experience in New York where property valued at \$17,000,000 for assessment was found to be valued at \$247,000,000 at probate,³ and by the law of Louisiana (1904), which provided for an exemption if an estate had paid due taxes in the lifetime of the decedent.

The President seems to restate the theory that the tax is a payment for protection:

¹ Message, 1903.

² Quoted in Bastable, "Public Finance," p. 597.

³ Mass. Labor Bulletin, January, 1907, p. 10.

"The man of great wealth owes a peculiar obligation to the State, because he derived special advantages from the mere existence of government. Not only should he recognize this obligation in the way he leads his daily life and in the way he earns and spends his money, but it should also be recognized by the way in which he pays for the protection the State gives him."¹

Although the political habit of imitation, the assumption of evasions, or of the political dishonesty of most large States, or other historical considerations may be as valid reasons for the tax as are the theoretical defenses of economists, a rational basis for any political system gives more consistency and more confidence to its execution. It is, therefore, not allowable to say that the increased tax is levied merely for the sake of revenue — that would be called confiscation. It may not be solely on the grounds of a more equitable redistribution of property, if it is desirable to avoid the charge of socialism. It is accordingly desirable to convince the man who is about to leave a considerable fortune and the man who is about to receive a considerable fortune that the estate is not inequitably treated by the exaction of an increasingly large portion, by the universal co-heir, the State. Since it is not infrequently impossible to convince interested individuals whose interest is part of the medium of their insight, it is desirable to convince the majority of those constituting a government of the political expediency of increasing taxation of inheritance.

Accordingly we say that an inheritance tax bearing disproportionately upon a great estate is not in violation of the principle of equality in taxation, if the principle of equality in government and in privilege is violated in the creation of great estates, or in the transmission of such estate to one without special industrial merit, and through the circumstances of the special extraneous aids of social increase, social sanction and political security. The decedent is no longer entitled to privileges of citizenship, because he has laid aside the duties of citizenship; the heir is not inequitably treated by an enforced division of the estate since he is about to be a violator of the principle of equality in being the recipient of a status in society which he

¹ Message, December, 1906.

has not earned, but which society, under the influence of his benefactor, has created for him.

It will be assumed that the increase of the tax must recognize the present American ideas and preserve private property with the consequential competitive business organization, and that even the right of an heir unentitled individually or by service shall be preserved. It does not matter that this latter right is illogical, when judged by our supposed philosophy of individualism. Illogicalness is one of the essentials of popular ideas.

No theory of property right can be devised which does not leave the exercise of property rights at the will of government. Is property a natural right? Is it allowed as a human individual necessity? It cannot then limit the living by the wish of the dead. Did prescription or occupation create and justify property on the ground of the right of the stronger? Prescription created also something stronger than the individual — the government. Do we base the theory of property on labor? Then it follows that government may take all it pleases from those who have not labored. If we say that property is the creation of law and government for the sake of its social utility, then it is emphatically subject to modification by its creator in order to adapt it to the exigencies of social evolution. No reasoning about the nature of justice can establish the right of property to be independent of government, not even that theory which explains best current ideas of justice and most defies government — the belief that justice is the right of the stronger. This would entail, indeed, the destruction of a property at the death of its possessor.

But property is a social creation in another important sense in that its increase is the result of social contribution. What are the constituents of a large property? Individual industry; this is so small an element that it is a forgotten cornerstone at the base of a large property. Individual sagacity; — in what else, but in seeing natural or social opportunity and in directing social effort or managing social patronage in realizing such an opportunity? Without social contribution of service and patronage there could be no large property. Nature without social coöperation cannot be conceived as producing any large fortune. Nature entails no individual claim and as a possession

is very limited in extent without social increase and social labor, that is, without the unearned increment. This applies to all forms of large gain alike. They are all created by social increase. It is especially true that the individual merit of the owner of industry is less under the established tendering toward monopoly, which, by restricting the ability of competitors, gives an easy advantage to owners in a monopoly. Most of our troublesome fortunes are the fruit not so much of industrial organization as of mere fortune or of shrewdness in effecting transfers of ownership. Society and nature owe no rewards to mere shrewdness, but only to service and enterprise. If, therefore, property is a social creation, — because society sanctions it and because it is the joint product of individual sagacity, the social increase and the economic tendency to organization, — it follows that it is subject to the exaction by its creator of a share of the fruits of social evolution and effort. A large inheritance tax is in its effects not different from any of the current great restrictions of property operations in the interest of justice. This seems to be recognized in the special appropriation in some of the States of revenue derived from this tax to distinctly social purposes, as to the State University in Missouri and in Idaho, and in the recommendation of the Governor of Louisiana that it be applied to the school fund.

Moreover, property is a political and social creation, which, once created, is inseparable in its scope and power from political and social sovereignty. This is a universal truth, not more true to Plato and in the feudal age than in the present time, notwithstanding the riotous academic theory of the past century. This is especially true under the present corporate or associated organization of society, in which less than ever before is due to the individual and more to the social productivity. Corporations have never lost their character as public bodies, save in the market-place mind. The President's advanced position is nothing more than an enforced, logical and practical and statesmanlike recognition of the public rights in great accumulations of economic and political power. From those who enjoy social privileges, which under legal and social security and the economical organization of corporations increases the power of the individual at a rate far exceeding the increase in his personal ability

and desert, society may exact a disproportionate tax, without infringing even upon the principle of equality in taxing according to ability. There are no excessive rights without excessive duties. It is not the individual alone who is growing in ability. It is an extraneous, social addition to himself. This justifies more than proportional contribution to society. If logic rather than force were the basis of social judgments, the man who protests against public exactions on the ground of individualism should also refrain from deriving profits from such essentially public and social processes as the enterprises of corporations. This fact of the economic and political power of wealthy men and their corresponding social obligations is recognized on all sides by wealthy men. Russell Sage said: "The chief responsibility of the man of wealth is in the using of his money for purposes that will do the greatest good to the greatest number in the creating of opportunities for the masses. The founding of great industries serves such a purpose."

J. J. Hill says: "Consolidation of wealth does not mean the hoarding of money in a bag. It is the effective organization of effort. No man grows wealthy along broad and legitimate lines without turning the resources of nature into remunerative channels of usefulness for the talents of other men."

In feudal theory the "relief" was not a tax on property, but a withholding of political power from a successor. That the inheritance tax recognizes still the relation of property to political power seems to find evidence in some of our legal procedure. Thus, Iowa (1904) taxes non-resident alien heirs 20 per cent, or four times the usual amount, thus taxing especially those who have the civil privileges without performing the political duties of ownership. The federal inheritance tax was upheld on the ground that it was not a regulation of inheritance or a tax, but an excise on the right to succeed to ownership.¹ An Ohio law is entitled "an act to impose a tax upon the right to succeed to or inherit property."

A large tax would leave a large amount of private property and the privilege of further freedom in acquisition and even the right to give to an unentitled heir a status in society far greater than that of the decedent, since the heir may start in economic

¹ *Scholey vs. Ren.* 23 Wall. 331.

power where the decedent left off. Thus our exercise of private rights are not destroyed — only civilized. The desire to thrive, be master and acquire, would not be discouraged, unless it shall become man's nature to prefer an inferior position. The inheritance tax is not a tax on thrift and industry any more than is any other tax. It is much more likely to be a tax on idleness than on thrift. The inheritance tax, by its imposition on property at a point where there is no owner, preserves individualistic ideas and entails the least real sacrifice. Thus, New Hampshire (1903) believed that "a tax on property, when passing by will or inheritance, might produce considerable revenue without injury to any one." The inheritance tax as now applied, and as it might still be applied under a vast extension of its amount, preserves the principle of family spirit, although our laws of inheritance and our other laws do this only to a limited extent. The right of bequest is contradictory to the right of inheritance. The laws of bequest do not fully preserve the supposed rights of direct heirs, while to distant relatives the possessor of a property recognizes usually no economic responsibility during his lifetime. Why then should the dead possessor be allowed to exercise as a privilege what while alive he denied as an obligation?

If it is allowed that society organized as government is superior to the individual as the subject of the government, and that social sanction is the only guarantee of property, society is generous indeed beyond the requirements of exact justice if it assesses enormous property on the principle of proportional equality while its possessor lives, and if, after some exactions, it allows the future possession the same privilege. For this is done at the cost of some strain on democratic principles. Under the present application of the principle in many of the States, particularly in the newer States, the law is important neither as a revenue producer nor as an influence for the preservation of democratic equality. Of the six far Northwestern States considered, Washington alone enjoys any appreciable revenue from inheritance taxation. Thus, in Montana, after ten years of operation of a tax of 1 per cent on direct heirs, of 5 per cent on collateral heirs, the revenue is less than 1 per cent of the State revenue, and about the same as that produced by the escheated

estates of the very poor. In 1905 the assessed valuation of property in Montana was \$209,912,340, while the revenue from inheritance tax for two years was but \$12,076, or less than ~~100,000~~ per cent of the assessed wealth of the State was thus transferred in two years. Hence there is no immediate cause for alarm at the progress of socialistic principles. If it is held desirable to maintain democratic government by securing democratic society, it has been shown that the progressive assessment of the inheritance tax is no more than a recognition of the more than proportionate extension of economic power with the increase of the external accretions of a man. In addition it may be urged that the principle of ability is regarded by progressive taxation, in that the measure of man's ability is not justly to be estimated by what he has contributed, but by what he has left, which may be rapidly growing disproportionately to the growth of other men's ability, even under the levy of a progressive tax. This represents the social tolerance which is the essence of property. Property is not in having, but in being allowed to have. Practically the justice of a tax progressive in amount both with the amount and with the distance of the heir from the decedent is recognized in many state laws and in many decisions.¹ The tax is progressive in most democratic countries. The same arguments and the same decisions that establish progressive taxation apply to highly progressive taxation and to the application of progressive taxation to direct as well as indirect heirs. The law is of no social value if it exempts direct heirs.

How, then, can the argument be carried this far without recognizing the logical conclusion,—“the ultimate limitation of the size of swollen fortunes”? Is there a just way of curbing rapacious opulence? Should a maximum figure be fixed by law above which the inheritance tax should be 100 per cent? Upon the basis of the argument from the principles of equality in taxation and the political character of property, it is not just to progressively increase the tax after one's inheritance reaches \$10,000, and so on to perhaps \$1,000,000, and then allow the progression to cease. This is the common practice, and it taxes the intermediate fortunes at a greater figure relative to ability

¹ *Magoun vs. Trust and Savings Bank*, 170 U.S. 283.

than those which are swollen. Thus under the last federal tax, a collateral inheritance of \$100,000 to \$500,000 paid 10 per cent; an inheritance of \$500,000 to \$1,000,000 paid 12½ per cent; while an inheritance of \$1,000,000 and over paid 15 per cent. What is left being the measure of the individual's power, why should a man who is allowed to keep 92.5 per cent of his first \$50,000, be allowed to keep only 90 per cent if he got another \$50,000, while the heir of \$50,000,000 should be allowed to keep 85 per cent of his fortune, and still to keep 85 per cent if it were \$100,000,000 or \$1,000,000,000?

Thus a relative exemption is allowed to the most troublesome fortunes, and if the tax is allowed to become anything more than a mere administrative measure, the principle of progression can be applied justly only if it is progressive to 100 per cent.

But expediency, not logic, governs taxation. If it should be admitted that progressive taxation of any degree is inequitable, it might be asked: How much more inequitable is it than the present incidence of indirect taxation, or than the present distribution between country property holders and town property holders? A large progressive tax would be a slight corrective of these injustices. Moreover, we have not the courage to proceed to the theoretically necessary 100 per cent tax. Expediency still admits a gradual and great extension of the principle. Further, if it be admitted that a tax on luxury is just, it is just to tax fortunes progressively without proceeding to the limit, since there is a limit of unproductive luxury beyond which even vast fortunes cannot go. Since I do not know as much about this subject as the distinguished gentlemen who are to discuss it, I may come boldly to conclusions without the caution or the fear that belongs to knowledge and experience.

All this sounds like *a priori* reasoning. Accordingly it may make no appeal to our friends whose basis of judgment is individual interest. What influence then will it have to state that the logic of history coincides with this reasoning and justifies some such reflection as that of the President of the United States? There is an unhealthy corpulence which cannot be seen as well by the corpulent as by a disinterested

on-looker. Reasoned theory is frequently the goal attained by unreasoned practice by a more circuitous route. It is unnecessary to prove to any but the opulent that relative equality in property is essential to relative democracy, and it cannot be proved to them. The modern inheritance tax is the spontaneous product of democracy, and the period of the general adoption of inheritance taxation coincides with the period in which democracy has been most threatened by opulence. Only four inheritance taxes, and these moderate, existed in the United States before 1885. They now exist in thirty-four States. This coincides with the period in which we have had various efforts to curb the semipolitical power of great accumulations of economic advantage. The facts of such taxation coincide with the period in which two presidents of the United States, one candidate for the presidency of the United States, and one United States senator, with the disinterested vision of statesmanship, have proposed outright limitation of the size of great fortunes. It is during this time that Pedro Alvarado proposed to give to the Republic of Mexico \$50,000,000, because he took his millions out of the ground, which belonged rather to the nation than to himself; and Senator Clark, of Montana, says that he holds a similar fortune for the benefit of the people; also, Mr. Baer says, "The rights and interests of the laboring men will be looked after and cared for, not by the agitators, but by the Christian men to whom God in his infinite wisdom has given the control of the property interests of the country." It is during this time that Alfred Nobel said, "Any man possessing a large fortune ought not to leave more than a small part of it to his heirs, not even to his direct heirs — just enough to make their way in the world." Andrew Carnegie said that 50 per cent is not too much for such a tax.¹ It is the generation which has seen private benefactions to the total of perhaps \$1,000,000,000. It is the generation which has seen public charities at the cost of taxes increase to nearly \$20,000,000 annually, and pensions from \$15,525,153.11, in 1866, to \$141,142,861.33, in 1905.

The desirability of extending the tax is seen in its actual extension, of which illustrations correspond almost with the

¹ Quoted by Ely in *North American Review*, Vol. 753, p. 62.

number of new acts. Thus, West Virginia increases rates from a uniform $2\frac{1}{2}$ per cent to 3 per cent, 5 per cent and $7\frac{1}{2}$ per cent. California adds the taxation of lineal descents and makes the tax progressive. The Pacific Northwestern States, where large fortunes have not yet acquired such great power to defeat legislation, tax lineal inheritances; and the Massachusetts governor recommends extension of the tax to direct heirs. From the recent laws of the Northwestern States of Montana, Oregon, Washington and Wyoming, may be recommended the extension of the taxation of direct inheritances.

The state treasurer of Montana, J. H. Rice, recommends to the consideration of this Conference that the tax be graded according to the amount left each heir, in order to encourage the cutting up of large fortunes; that the gradation be as follows:

AMOUNT OF INHERITANCE	DIRECT HEIRS	INDIRECT HEIRS
Over \$5,000	1%	5 %
Over \$50,000	2%	$7\frac{1}{2}$ %
Over \$100,000	3%	10 %
Over \$500,000	4%	$12\frac{1}{2}$ %
Over \$1,000,000	5%	15 %

This decreases the exemptions from the present \$7500 for direct inheritance. From the practice of the Pacific Northwestern States, a rather high exemption of \$10,000 for direct inheritance, or even the \$20,000 and \$25,000 exemptions of South Dakota and North Dakota, may be recommended as just, and especially if there is to be a relative upper exemption.

The tendency to exempt public and benevolent institutions, as in recent laws of West Virginia, Tennessee, Maine, Pennsylvania, and in the Pacific Northwestern States, is perhaps a recognition of the distributive purpose of inheritance taxation. North Dakota, however, exempts nothing. The state treasurer of Montana recommends that nothing be exempt but state institutions. The desirability of this depends upon the desirability of extending state functions.

As to appropriation of the revenue, it seems that this is a state revenue rather than a national revenue, — since the national effort to add to inheritance taxes evidently resulted in confusion, and sometimes in inequitable burdens; since the jurisdiction which bears the burden of protecting the estate is entitled to its revenue and might prevent its withdrawal from the State; since the community in which the estate is situated, and in which its owner received benefits, is more interested in its contributions to social ends; and because the conditions prevailing in all States do not justify the same treatment in all cases, and because the States have already appropriated this means of revenue.

Washington, Idaho, Wyoming and North Dakota apply the entire revenue to the state fund. Montana recommends its division of the revenue: 60 per cent to the State, 40 per cent to the county; and the coöperation of the State with the county in administration. The division secures wider interest in an honest collection and avoids county connivance with the citizens of the county in evasions, while retaining local interest. The officials of all these Northwestern States agreed that there is little evasion of the tax. In Montana the administration is in the hands of the clerk of the district court and the county treasurer. In Idaho the county attorney may institute proceedings in the probate court if the tax is not paid to the county treasurer on demand. Where the revenue is important, the interest of the State might be secured against evasion by a state examiner or other officer. Idaho recommends that the state authorities should have a more direct supervision of its collection. In Washington the collection is in the hands of the State Board of Tax Commissioners. This board recommends that the state commission be served in one notice with dates of filing of applications for probate, list of heirs and their relationships, and of the appointment of appraisers, with the time and place of appraisal. The tax should be paid through the commission, in order that check might be kept upon the state treasurer's office.

This commission also asks the court having jurisdiction of the estate to enter an order approving its appraisal, fixing

the amount of the inheritance tax and directing the payment by the administrator or executor.

This board recommends further that the state should be represented at the appraisement in order to prevent evasions by under appraisement. Governor La Follette,¹ of Wisconsin, says that "some effective supervision on behalf of the State is necessary to insure to the State its lawful revenues," and recommends that the State be represented by an attorney detailed from the office of the attorney general.

¹ Message, Jan. 12, 1905.

TAXATION OF INHERITANCES

BY DR. MAX WEST

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DURING the past few years there has been a remarkable development of inheritance taxes, not only in the United States, but also in the most important countries of Europe — a development in the direction of progressive rates rising to very high percentages. Fifteen years ago progressive inheritance taxes were almost unknown outside of Switzerland and Australasia, though in Great Britain the death duties were very slightly progressive, and the Canadian provinces were just beginning to follow the example of the Australian colonies. To-day elaborate progressive scales, with maximum rates of from 20 to 25 per cent, are found in Great Britain, France, Germany and Italy, as well as in several of the Swiss cantons; and even in Russia progressive rates have been seriously proposed by the government.

In France the maximum rates, applying to the excess above 50,000,000 francs received by each heir, range from 5 per cent for direct heirs to 20½ per cent for very distant relatives and bequests to strangers in blood. Last year the finance minister, M. Poincaré, proposed a still more rigorous application of the progressive principle to large inheritances, which would have made the maximum more than 31 per cent; but this proposal was rejected by the Budget Committee.

In Italy the progressive scale is similar to the French in form, but the maximum rates of 3.6 per cent for direct heirs and 22 per cent for distant relatives and strangers apply to the excess above 1,000,000 lire of each inheritance.

The German inheritance-tax law of 1906 is of special interest because it marks the appropriation by the imperial government of a form of taxation formerly left exclusively to the separate States of the Empire. The progressive scale rises to a maximum of 25 per cent for amounts of more than 1,000,000 marks

passing to distant relatives or strangers in blood. On amounts in excess of 1,000,000 marks the German tax is much heavier than the French, partly because the maximum rates apply to the entire inheritance, and not simply to the excess above the next lower class in the progressive scale, as in France. On the other hand, the German tax does not apply to children or other direct descendants, though the separate States still have the privilege of taxing direct inheritances, as a few of them did before the imperial tax was imposed. One third of the proceeds of the imperial tax goes to the separate States, in proportion to the amount collected in each; and as this tax is expected to yield nearly three times as much revenue as the state taxes did, the States will be nearly as well off as before, on the average, even without levying additional taxes.

It is already well known that the British Finance Act of 1894 imposed a progressive estate duty rising to a maximum of 8 per cent, in addition to the previously existing legacy and succession duties with their maximum of 10 per cent. The Finance Act of 1907 increased the rates of estate duty on large estates. On estates of more than £1,000,000 in value the rates are now 10 per cent on the first million pounds and from 11 to 15 per cent on the remainder, making the resultant rate nearly 14 per cent for all estates of more than £3,000,000. With the addition of legacy and succession duties, any part of an estate of more than £3,000,000 passing to distant relatives or strangers will pay about 23 per cent in death duties; and the high rates of the estate duty make the maximum tax demanded of direct heirs higher than in any other country.

All the more important Canadian provinces now have progressive inheritance taxes, the maximum rates for direct heirs ranging from $2\frac{1}{2}$ to 10 per cent, and for distant relatives from $7\frac{1}{2}$ to 15 per cent, though the most common maximum is 10 per cent. In most cases there are light probate fees in addition to these progressive taxes.

Nowhere has the development of inheritance taxes in recent years been more rapid than in the United States. Fifteen years ago such taxes were found in only nine of the States, extending geographically from Massachusetts to Tennessee. In every case they were collateral inheritance taxes only, except

that the New York tax had been extended to direct inheritances of personal property; and nowhere did the rate exceed 5 per cent. Since then not only have a majority of the States adopted this form of taxation, but in many cases the tax has been applied to direct as well as collateral heirs, and the progressive principle, first adopted by the Ohio legislature, in 1894, but vetoed by the Supreme Court of the State, has been introduced, with better success, in a number of other States. Inheritances are now taxed to a greater or less extent in thirty-six States of the Union, and in Hawaii and Porto Rico. Twenty States of the Union tax both direct and collateral heirs; and in thirteen States the inheritance tax is in some degree progressive. Wisconsin, California, Idaho, Minnesota and Massachusetts have progressive rates for both direct and collateral heirs; in Illinois, Colorado, Nebraska, South Dakota, Oregon and North Carolina the progressive rates apply only to distant relatives and strangers in blood, while in Washington and Texas they apply to all collateral heirs. Minnesota and Utah make no distinction between direct and collateral heirs; in all other cases in which direct heirs are taxed at all the rates are much lower and the exemption, as a rule, much more generous than for collateral heirs. In several cases direct heirs have a \$10,000 exemption; in Illinois and West Virginia, \$20,000; while in Wyoming the surviving husband or wife and children, if residents of that state, are favored with an exemption of \$25,000 each. Washington and Iowa discriminate against alien non-resident heirs. In Michigan and Montana the direct inheritance taxes still apply only to personal property.

The Illinois inheritance tax, adopted in 1895, is noteworthy because in upholding it the Supreme Court of the United States practically sustained the constitutionality of progressive taxation in general; and also because its provisions have been adopted with some modification in several other Western States. The Illinois act provides for a tax of 1 per cent on the excess above \$20,000 received by each direct heir, brother or sister, son-in-law or daughter-in-law, and by the surviving husband or wife; a tax of 2 per cent on the excess above \$2000 received by an uncle or aunt, nephew or niece of the decedent, or any descendant of such relatives; and a progressive tax of from

three to six per cent, according to amount, for more distant relatives and strangers in blood.

The Wisconsin act of 1903, which has been copied with but few changes by California and Idaho, provides for progressive rates for both collateral and direct heirs. The primary rates ranging from 1 to 5 per cent, according to relationship, are multiplied by $1\frac{1}{2}$, 2, $2\frac{1}{2}$ and 3 for the excess of each inheritance above \$25,000, \$50,000, \$100,000 and \$500,000, respectively, making the maximum rates 3 per cent for direct heirs and 15 per cent for distant relatives and strangers. The surviving widow is taxed only on the excess above \$10,000 (California and Idaho extend this generous exemption also to minor children); as the rate increases with the remoteness of relationship, the exemption diminishes.

Specially worthy of mention also are the Washington law of 1901 and the Texas act adopted this year. Each imposes a progressive tax on collateral heirs with a maximum rate of 12 per cent, which in Texas applies only to the excess above half a million dollars, but in Washington applies to any excess above \$100,000. In Washington there is also a 1 per cent tax on direct heirs; but in Texas direct heirs are exempt.

Massachusetts and West Virginia, which have had collateral inheritance taxes for some years, have only this year extended them to direct heirs; and in Massachusetts progressive rates were introduced at the same time, but the maximum rate is only 5 per cent, the rate which applied to collateral heirs before.

The Spanish War gave us a national tax on legacies and distributive shares of personal property, graduated from $\frac{1}{4}$ of 1 per cent for amounts under \$25,000 passing to direct heirs, to 15 per cent for amounts of more than \$1,000,000 passing to distant relatives or strangers. In 1901 North Carolina adopted a tax with a similar progressive scale. For a year or more, therefore, it was possible for large amounts of personal property in North Carolina passing to distant relatives to have to pay practically 30 per cent to the national and state governments together, while in Washington the total might have been nearly 27 per cent ¹

¹ Since it was the practice of the national government to tax only what was left after the state tax had been paid, the actual maximum rates were a little less than the percentage named.

— both higher rates than are in force in any considerable country in the world. But the national tax was repealed in 1902.

The rapid extension among the States of progressive inheritance taxes, in several cases with such high maximum rates as 12 or 15 per cent, and still higher rates in European countries, suggests that the taxation of inheritances is perhaps being resorted to as a means of preventing the perpetuation of very large fortunes in their entirety, rather than as a purely fiscal measure. Yet it is by no means necessary to consider the inheritance tax, even with these high rates, a limitation of inheritance. The argument most frequently heard in this country in favor of this form of taxation, at least until within a year or two, has been based upon the ease with which the personal-property tax is evaded by owners of large amounts of easily concealed personal property. In other words, the inheritance tax has been regarded by many legislators as a property tax, paid once for all at death in lieu of the taxes evaded during life; and this explains why it has in some cases been restricted to personal property. Louisiana carries this idea to its logical conclusion by exempting all property which has borne its just proportion of taxes prior to the time of the inheritance; yet, strange to say, the inheritance tax is fully as productive in Louisiana as in a good many other States.

If the inheritance tax, which is paid but once in a generation, be imposed in lieu of an annual property tax, the rate might logically be thirty-three times as high as the usual property-tax rate; or if it be imposed in addition to a property tax and in lieu of the taxes which are evaded, still a rate on personal property as high as 25 or 30 per cent might readily be defended. From this it follows that considered merely as a substitute for annual property taxes which it has not been practicable to collect during the lifetime of the owners a progressive inheritance tax on both real and personal property may rise to a maximum rate of 12 or 15 per cent on the excess of each inheritance above half a million dollars, as some of the American taxes do, without being excessive. The progressive rate may be defended on the ground that the wealthy are able to conceal more of their wealth than the comparatively poor. An inherit-

ance tax, even a progressive tax, with a maximum of 15 per cent is not a very effective limitation of inheritances, whatever we may think of the desirability of such limitation.

In conclusion, I wish to call attention to a very practical problem immediately confronting the States, growing out of interstate double taxation, a problem which has already been referred to more than once. There is if possible a more pressing need for a solution of the problem with reference to the inheritance tax than with reference to the property tax, because in the latter case the chances are that personal property in one State belonging to a resident in another State will escape the assessor in one place or the other, if not in both. But in the case of the inheritance tax, it often actually happens that personal property is included in the appraisals both where it is kept and where the owner lived during his life; and if it consists of stock in a corporation it may be reached also at the corporation's home office, for some of the States make their corporations responsible for the tax on any stock transferred on their books at the owner's death.

A few States make some attempt to solve the problem by means of reciprocal provisions similar to the Ontario plan, to which reference was made yesterday. Thus the West Virginia law provides that inheritance taxes due to another State or country on personal property therein are to be deducted from the tax otherwise payable in West Virginia, and the personalty in West Virginia of non-resident decedents is exempt in so far as the State or country of residence exempts the personalty of West Virginians. Vermont goes even further and unconditionally deducts any inheritance tax lawfully paid elsewhere. Massachusetts has this year adopted a plan similar to that of West Virginia, and in addition an interesting experiment with reference to the stock of public-service corporations. Shares of non-resident decedents in a railroad, street railway, telegraph or telephone company incorporated in Massachusetts and also in another State are considered within the jurisdiction of Massachusetts only to the extent that the line is in that State. In other words, the tax is divided according to mileage.

But while a few States are making an effort to avoid double taxation, the majority still include in their inheritance-tax

appraisals property within the State regardless of the owner's residence, and also the property of resident decedents wherever situated. There is urgent need of some form of interstate action, or at least a more general adoption of reciprocal provisions such as have been referred to, in order to avoid double taxation. To promote interstate comity in these matters should be one of the functions of tax conferences like this, at which the various States are officially represented.

THE POSITION OF THE INHERITANCE TAX IN AMERICAN TAXATION

BY PROFESSOR CHARLES J. BULLOCK

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To Americans of the last generation the inheritance tax was a fiscal curiosity. It had been adopted by Pennsylvania in 1826, and subsequently had found its way into a few other States. But most of these early experiments came to untimely ends, and a "legacy tax" enacted by the national government in 1862 met with a similar fate when internal taxation was reduced after the Civil War. Prior to 1885 the net results of all efforts to domesticate this tax in the United States had been that two States, Pennsylvania and Maryland, were then levying light duties upon collateral inheritances. In that year, however, New York established a tax upon collateral inheritances, which, in 1891, was extended to direct inheritances of personal property; and her example was soon followed by other States. In 1894 Pennsylvania and Maryland had collected \$663,000 from inheritance taxes; in 1892 six States collected \$3,107,000. Ten years later twenty-eight States drew \$7,138,000 of revenue from this source, and in 1905 thirty States received approximately \$10,600,000. At the present moment the inheritance tax is found in not less than thirty-four States, and in nineteen of these it applies to direct inheritances as well as to collateral. Manifestly the taxation of inheritance is no longer a debatable issue, but must be accepted as an accomplished fact of American finance.

But widespread acceptance of the tax itself has not brought uniformity of legislation, or even agreement concerning its true position and function in our American system of taxation. Without doubt reasonable uniformity is desirable here, as at many other points in the domain of state legislation; but I have preferred to invite your attention to the second subject,

believing it to be of more fundamental and vital importance. What then is the proper function of the inheritance tax, and what should be its position in our general scheme of taxation?

In considering the proper function of the inheritance tax we are brought directly to the question whether it should be employed solely for the purpose of raising revenue, or should be used as a means of regulating the distribution of wealth. In the laws now on the statute books of the several States the controlling purpose is, clearly, to raise revenue. Upon direct inheritances the rates range usually from 1 to 3 per cent, and in no case exceed 5 per cent; while upon collateral they seldom rise above 6 per cent. These figures are not higher than can be justified on purely financial grounds; in fact, in many States the rates are less than the experience of other countries shows that the legislature might well impose. They yield considerable revenue which can be collected with reasonable certainty, slight expense and comparatively little hardship to taxpayers. Upon estates of the largest size passing to distant heirs or strangers in blood, the tax sometimes rises to 15 or 20 per cent; but occasion seldom offers for the application of such high rates, and even then the limits set by sound principles of finance are not overstepped. A tax of 20 per cent upon property in excess of \$500,000 passing to unknown relatives or strangers in blood, may appear startling at first thought, yet it may be defensible from the purely fiscal point of view, and will exert little influence upon the distribution of wealth in the United States. Upon most inheritances, collateral as well as direct, we are now levying from 1 to 5 per cent. On the theory that the purpose of the laws is to raise revenue these rates can be readily understood; they are altogether ridiculous, if we assume that the purpose is to modify perceptibly the distribution of wealth.

But the proposal is now made that we should change the theory and practice of inheritance taxation in order to secure greater equality of wealth and opportunity. This has long been the view of that eminent German economist, Professor Wagner, and others of his school. In this country it has recently been projected — not to say precipitated — into the field of political discussion. The suggestion is made that

existing conditions have led to the growth of enormous fortunes far exceeding any service the recipients have rendered to society; and it is urged that the time has come to levy progressive income and inheritance taxes in order to reduce these fortunes to a normal size. Absolute equality is not proposed as an ideal, but no definite suggestion is vouchsafed concerning the amount of reduction that is desirable. And finally, it is declared that the work belongs properly to the federal government and not to the several States.

Concerning the last matter there can be no difference of opinion. If swollen fortunes are to be reduced to reasonable size by inheritance taxation, the rate imposed upon all successions, direct even more than collateral, must be raised to a very high figure. From 2 or 3 per cent the tax levied upon large estates must advance to 10, 20, or 30 per cent, and perhaps more, before it can have the desired effect; and it must apply to property passing from husband to wife, father to child, or brother to sister. Now it is not to be supposed that all the States will be convinced simultaneously that such radical action is necessary; and if some refuse to follow the lead of the others, it is easy to see that there will ensue, and that speedily, a fearful congestion of swollen fortunes in a few unprogressive but prosperous States. He who doubts this prediction has only to inquire in what States the corporations are now chartered from which the "undesirable" fortunes have been mainly drawn. Of a certainty, then, the work is too large for the several States, and calls for the interposition of the national government.

What now shall be said of the main proposal? Is it desirable to employ the inheritance tax as an instrument for reducing swollen fortunes? The question assumes that there is in the United States an undue concentration of wealth and power in a few hands; and that such is the case, I should be one of the last to deny. It has long been evident to thoughtful men that enormous fortunes have been created through special privileges accorded by the law or wrested from the people in defiance of all law. A few years ago this statement might have needed to be supported by a bill of particulars, but to-day it will be as readily understood as if I were to refer you to facts

judicially ascertained in courts of law, or brought to light by the Bureau of Corporations and Interstate Commerce Commission. Fortunately the country is thoroughly alive to the situation, and is turning to the problem with a normal earnestness which augurs well for a reasonable solution. In the alarm and righteous indignation aroused by recent disclosures it is not strange that many persons should be ready to strike at offending individuals and corporations with any weapon that may chance to be at hand. But with all respect to the high source from which the suggestion has come, I am constrained to believe that the inheritance tax is not the instrument to employ.

For, in the first place, a retributive inheritance tax could only remedy some of the ill effects of undue concentration of wealth, and would in no way remove the causes. In social therapeutics, as in medical, it is sound policy to aim at causes rather than effects; and this case is no exception to the rule.

If fortunes have been made by reckless or dishonest management of large corporations, the obvious remedies are, reform of our corporation laws and the cultivation of higher standards of business morals. This may be a slow and difficult task; but it is perhaps *the* issue of the hour, and beside it the taxation of inheritances pales into utter insignificance. New legislation will be needed, but the relentless enforcement of existing laws against such old-fashioned offenses as conspiracy and theft would probably go far to accomplish the desired result. Make it as dangerous to mismanage a transcontinental railway as to hold up a transcontinental express, and you will speedily reduce one class of swollen fortunes. Make it as perilous for an officer to plunder an insurance company as for a clerk to appropriate a few hundred dollars from its funds, and you will reduce another. Punish the financier who loots a street railway as you punish the hungry man who robs a bakery, and you will reach a third class of fortunes. Deal with such gentlemen in the criminal courts rather than in the probate, and you will remove causes of dissatisfaction; pursue them in the civil courts with suits for restitution, and you will return stolen goods to the rightful owners. These remedies are simple and old-fashioned; they may offer no complex problems for the

amateur sociologist; but they lie directly at hand, and have a potency far exceeding all schemes for social regeneration through act of Congress.

And so it will prove with the other causes of discontent. Few things have aroused more alarm and resentment than the discovery that the railroads of the country, for more than a generation, have been aiding large corporations to destroy the business of their competitors. This evil our people are determined to eradicate, and they are finding that the remedy is to prosecute the chief offenders and make the punishment proportionate to the crime. In pursuing this policy, I submit, we are fairly on the way toward removing another cause of undue concentration of wealth; and I maintain that this is the only way in which we should proceed. It is cold comfort for the producer crushed by railroad discriminations to know that, through a graduated inheritance tax, the swollen profits of some trust will go to reduce the tax bills of the next generation. He is entitled to use the public highways known as railroads upon the same terms as the largest corporation; and if you will secure this right to him, his competition will provide you with a better remedy than any government can devise for undue concentration of wealth arising from the power to charge monopoly prices.

Another cause of discontent is found in certain schedules of the present tariff. It has always been the theory of the protectionist that, after foreign competition is restricted, the competition of domestic producers will establish a fair price for the product; and it is too clear for controversy that the formation of close combinations among protected manufacturers destroys the very basis of the argument. It is not surprising, therefore, that confirmed protectionists — of the wicked free-traders I now say nothing — are demanding a revision of the present tariff; and insist that revision, when it comes, shall this time proceed in a downward, not an upward direction. Here again, I submit, the country is turning to a simple, straightforward, and effectual method of preventing undue concentration of wealth. It is, assuredly, a singular policy which leaves on the statute book a law that tends to create swollen fortunes, and then establishes an inheritance tax in order to recover for a

future generation some portion of the tribute exacted from the present.

Another source of the swollen fortunes about which complaint is made is the exploitation of public franchises by private corporations engaged in so-called municipal monopolies. I cannot dwell upon the subject, but merely suggest that here, too, we are beginning to apply the natural remedy, which is effective control of public-service corporations. This policy, if consistently followed, will deal directly and effectually with evils for which an inheritance tax would afford but partial and tardy relief. Here, as elsewhere, a straightforward course is the easiest and best. In the body politic, as in the body human, we should eradicate the causes of disease rather than seek heroic remedies for mere symptoms. If for a single generation we punish commercial crime, extirpate social brigandage, and abolish privilege resting upon unwise legislation, we shall probably find that the question of the distribution of wealth will have settled itself.

A second objection to the proposed employment of the inheritance tax is that it would punish the just man with the unjust, and would check legitimate ambition and business enterprises. For your tax law must be impersonal, and cannot be so drawn that it will apply to "*tainted*" fortunes only. You must enact that *all* fortunes in excess of a stated sum shall be liable to a tax of 10, 20, 50 per cent; and thus you punish the innocent as well as the guilty. You might, indeed, proceed upon the principle that no man can honestly acquire more than one, or five, or ten million dollars; that theory is sometimes propounded by persons who desire to regulate the distribution of wealth. But in that case you would be bound logically to levy a tax of 100 per cent upon all sums which wealthy malefactors accumulate in excess of the stated amount; otherwise you would refuse to recover for the use of all the people some portion of the property of which they had been despoiled, and would virtually connive at the transfer of stolen goods. If this theory proves more than is usually anticipated or intended, one, and only one, other may be adopted. We may proceed upon the theory that although a man may acquire honestly more than one, or ten, or twenty million dollars, it is undesirable

that he should be permitted to transmit such a sum to his heirs. Not unnaturally, this idea appeals strongly to those who believe that no small part of such swollen fortunes is likely to have been gained by methods which, if within the letter of the law, were contrary to sound morals and sound public policy. Without doubt it is upon such considerations that most advocates of confiscatory inheritance taxes would rest their case.

But even in this form the proposal is open to the objection that it contemplates the establishment of a hard and fast rule which must be the same for fortunes honestly acquired and for those gained through craft, deceit or oppression. Now what will be the effect of enacting that no man, however honest or able, shall bequeath to wife, or child, or other relative, more than a stated sum? This question is, perhaps, of a somewhat speculative character, and assumes that it is practicable to enforce such limitation by means of an inheritance tax. But if we assume that the regulation can be made effectual, is it not probable that the result would be to limit that enterprise and ambition upon which we now depend for all the larger things in the world of industry and commerce? I merely raise the question, for I have no time to argue it; and with it propose another, Would it not be expedient to postpone experiments with the equalization of fortunes, until we learn whether other remedies that lie ready at hand will not settle the problems of distribution to our reasonable satisfaction?

A third objection is that taxation, even the taxation of inheritance, is usually a clumsy agency for social reform, and ordinarily accomplishes either more or less than is desired. Our present moderate taxes of from 1 to 3 per cent upon direct inheritances are collected with considerable success, since it is found that the average man will not exert himself to escape them. He accepts them as a not unreasonable method of collecting revenue, and does not look upon the probate court as an agency for confiscating his fortune. But no experience of what wealthy men do under our present laws can justify us in concluding that they will not make every possible effort to escape a tax of 20 or 30 per cent, and no one knows how much more. For any State to collect such a tax would be substantially an impossibility, except in the case of landed property.

A federal tax would not be so easy to escape, but it is certain that various methods of evasion could and would be devised.

For under modern conditions capital knows no national boundaries, and when facing a confiscatory tax is generally free to migrate. Many capitalists, too, and those the largest, whom the social reformer desires most to reach, would choose expatriation rather than surrender, even at death, one third or one half of their fortune. Transfers of property long before death would become exceedingly common, and these could be controlled only by a universal system of taxes on transfers, than which nothing could be a greater impediment to legitimate business. Already one hears of trust companies in States levying no inheritance taxes that find a lucrative business in the management of property subject to taxation in other States; and it is not hard to conceive of the organization of such concerns in Canada, Mexico, or elsewhere, to offer similar facilities to Americans seeking escape from confiscatory federal taxation. And all this is not mere speculation. In France the rates are already so high as to encourage evasion, although they are supplemented by onerous taxes on transfers between the living. Bequests from father to child may be taxed as much as 5 per cent; property passing from husband to wife may pay as much as 9 per cent; and bequests from brother to sister may be assessed 14 per cent. These are the maximum rates, which fall only upon the largest estates; but the general scale is so high as to lead to much evasion, which is a subject of current discussion in France. The devices employed are explained by M. Guilmard in a recent book devoted expressly to the subject.¹ Fathers and sons open joint accounts in Swiss banks, and at the death of the former the property passes to the latter without the knowledge of tax collectors in France. And this, be it observed, occurs under a national tax, and one which is far lighter than that which we should need in order to reduce swollen fortunes. Can we doubt that a confiscatory federal tax would be subject to wholesale evasion, and that the very persons the reformer desires to reach would be best able to profit thereby?

The constitutional aspects of an attempt to reduce large

¹ E. Guilmard, "*L'évasion fiscale*" (Paris, 1907).

fortunes I am compelled to pass without remarks. If they have ever been considered by advocates of the plan, they have evidently been dismissed without serious study, perhaps as trifles about which the law does not care. I am unable, also, to consider the question whether, if the rights of inheritance and bequest are to be restricted, we would not better proceed by modifying the general laws relating to the subject, rather than educate men in the belief that they possess comparative freedom of testamentary bequest, and then undertake by taxation to prevent them from exercising that right. I venture, however, to express the opinion that, if this step is ever to be taken, the simpler, surer, yes, the honester, plan is to modify the laws of inheritance and bequest. Unless we are ready to do that, let us use the inheritance tax merely for the purpose of collecting a reasonable revenue from property passing in accordance with law.

It remains to consider the position of the inheritance tax in our American system of taxation. Should it be a state tax or a federal tax? Should it, possibly, be levied by both federal and state governments?

Until very recently the practice of other federal governments seemed to confirm the wisdom of our own. In Germany and Switzerland, as in the United States, the inheritance tax was employed by the several States or cantons; and the federal government raised its revenue by other taxes. But last year the German Empire established a tax upon inheritances which imposes even higher rates than were levied by most of the German States. This action breaks with the accepted practice of federal governments, and has been cited as a precedent for establishing a similar tax in the United States.

It is not difficult to show, however, that even if it is wise for the German Empire to tax inheritances, it by no means follows that our national government should pursue a similar course. This is a case where the financial conditions of two countries are absolutely different, so that the policy of one would be anything but wise for the other. In Germany the tax systems of the several States have been radically reformed in recent years, so that they offer, perhaps, the nearest approach to a scientific plan of taxation that can be found in any country of

the world. Upon the other hand, political and constitutional difficulties have prevented the imperial government from establishing an effective system of federal taxation. I cannot dwell upon the subject, and must simply remind you that in Germany the growth of imperial expenditures and the unsatisfactory outcome of indirect taxation brought it about that the imperial government was in sore need of revenue; and could, therefore, justify its appropriation of a share of the income obtainable from taxing inheritances.

I need hardly argue that in the United States the conditions are diametrically reversed. From the very beginning the federal government has ordinarily contrived to defray its expenses by indirect taxes, and it has to-day no occasion to appropriate any branches of taxation employed by the several States. True, national expenditures have increased in recent years, and are still rising. True, also, increased revenues may be needed before long. But even when that time comes there will be no need of taxing inheritances. By raising the taxes on beer and tobacco to the rates enforced during the Spanish War, and by reintroducing a moderate duty upon tea, not less than one hundred millions of additional revenue can be had without injury to business or serious burden to taxpayers. In this country, unlike Germany, only the state and local governments are seriously vexed with problems of revenue. From some branches of taxation they are debarred by constitutional restraints; from others, by economic; while their expenditures far exceed the total federal outlay, and bid fair to increase still more rapidly. Their taxes fall heavily upon property and business, and are usually so high that it is unwise, even if possible, to increase them. All the revenue that can properly be raised by the taxation of inheritances is sorely needed by the several States, and of right should be left to them. For the federal government to enter this field would be worse than a blunder, it would be a fiscal crime.

For financial reasons, therefore, I hold that the inheritance tax should be reserved for the several States. For economic and social reasons, I maintain, its function should be to raise revenue, and not to reshape the distribution of wealth. Upon both financial and economic grounds, I contend, we should not employ the tax in hazardous schemes for the regulation of fortunes.

THE TAXATION OF INCOMES

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THAT the citizen's ability to pay taxes to his State should be the correct and the only principle of taxation is now, I think, fully accepted. That one should make his contribution to his State in strict proportion to his ability is demanded by the very nature of his relationship to the State. He is an essential element of the State, just as the State is a fundamental element in his life and development. When the citizen pays his taxes, he should do it with the conviction of making a just contribution to the organized body of his fellow-citizens; and when the State asks for taxes, it should always be under the conviction of making a just request for aid from its members. This should, as I conceive it, always be our ideal of taxation, even though at present not one of us out of a thousand makes any serious attempt to realize such an ideal.

But closely and vitally connected with the citizen's ability to pay, and largely incorporated in his ability, is, I think, the benefit which the State bestows upon its citizens. Ability to pay taxes depends upon the general conditions of wealth production which the State, through the performance of its protective and developmental functions, creates and maintains, as well as upon the citizen's activity and effort to produce wealth. The ability-to-pay theory of taxation is then always to be supplemented by the benefit theory. Taxation upon the principle of the State taking from the citizen whatever it can take, irrespective of the ability to pay which he possesses, and irrespective of the general benefits which accrue to him from the State — a principle of taxation in great vogue even now when we take upon ourselves much pains to boast of our political fairness and honesty — has no rational defense whatever.

But what is the surest and most equitable measure of the citizen's ability to pay taxes?

The income of the individual citizen is, I think, the only basis upon which in theory the tax can be levied upon him with justice, however difficult this may be in practice; his income is, in the main, if perchance this can ever be accurately ascertained, the fairest measure of his ability to pay and of the general benefits which come to him from his State. And the income of the corporate citizen, that which in popular speech is known as the corporation, is likewise a most important basis of the taxation of the corporation, though not perhaps the only just basis. The corporate citizen occupies a relationship to the State which is in some particulars different from that of the individual citizen's rights to produce wealth. Though I do not think that this difference is very vital, even though I am much inclined to think that this difference is very slight, I would still, for the present at least, advocate that we continue to make two classes of income taxes: a tax on the individual's income, to be called in popular speech the income tax; a tax on the income and franchise of the corporation, to be called the corporation tax. In either case, that of the individual citizen, or that of the corporate citizen, it is the State, not the national government, which occupies the closest and most vital relations. These taxes, income and corporation, should then be left to the States as their exclusive sources of public revenue. At the present, and most probably for a time in the future, the federal government should confine its sources of public revenue to excises and customs, taxes which from their very nature cannot properly belong to the States.

What of a state tax on inheritance — a tax which is now in the eyes of the mighty public rapidly acquiring great importance? After the thing inherited has become an actual possession of the citizen, its income is, of course, included in his regular income and is taxed as such. But shall the mere act of inheritance be taxed? Shall it be taxed by the State, not the national or local government? Such a tax cannot, of course, be based upon the simple principle of ability to pay. This tax is not a question of the citizen's ability to pay, but of his coming into the possession of a certain property by the right of inherit-

ance; its principle is that of the benefit from the State to the citizen. The only theory upon which such a tax can rest is that the citizen never owns property in an absolute sense, but only relative to the rights of his fellow-men as they are organized in a social body — a theory the validity of which I am inclined to doubt. This theory contends that, when the citizen dies, his property belongs in part to this social body, only in part to him to whom he specifically transmits it. And it is the State, rather than the national government, or that of the local, which occupies the most vital relations with the citizen during the making of the property which is now transferred to another citizen by the right of inheritance, and consequently, if any civic body has the right to levy an inheritance tax, it is the State.

And what of land values as a source of state revenue? Land values are, in the main, more vitally related to the local government than to the state or the national. They should then, in theory, be left to the local government. But suppose that at times, and under certain industrial conditions, like those of a primitive agricultural life, it is from the point of view of the administration of taxes very difficult, if not indeed impossible, for the State to collect a sufficient revenue from individual incomes, corporations and inheritances. Shall not the State then levy a tax upon land values? While land values, as I see it, should, in the main, be left to the local governments as their chief, if not indeed their exclusive, source of public revenue, it may at times be wise for the State to collect a certain amount, even a relatively large amount, of its revenue from these values. When the industrial conditions are so primitive, and when the intelligence of the citizenship of the country is so slight — and such crude conditions are not at all unknown in many parts of our country — that from the point of view of the administration it is practically impossible for the State to secure a sufficient revenue from taxes upon incomes and corporations, then it is wise for the State to resort for a time to taxes upon land values.

My ideal for state taxation is, then, for it to make the taxes upon incomes (of individuals), upon corporations, and perhaps upon inheritances, as the chief source of its revenue, and to resort to taxes upon land values only when it is absolutely

necessary, and then only for a time. And I cannot but think that this ideal is more or less practicable, even though it be the ideal of a theorist rather than a practical statesman.

It is now necessary for me to discuss, with some detail, the method which shall be employed by the State in the taxation of incomes. What shall be taken, gross income or net income, as the fairest measure of the citizen's ability to pay? In theory it is the net income, rather than gross, that offers the fairest test of ability to pay. Gross income does not, as we well know, by any means always bear the same ratio to the expenses of its making. At times and in certain groups of wealth production the gross income is large as compared with the cost of its making, while at other times and in other groups of production it is small. Net income, that which is left after all the expenses of its making have been deducted, is then the fair theoretical basis of the citizen's ability to pay. But, from the administrator's points of view, it is oftentimes exceedingly difficult to ascertain, even approximately, what the citizen's net income is. So few are the individuals who keep their accounts of expenses and income with sufficient accuracy as to make it possible for the tax lister to ascertain their net income. The citizen most often does not know it, and the tax lister, who is not infrequently a man with slight intelligence and judgment, cannot possibly calculate it. But, while this is true from the point of view of the administration of the tax, still the ideal is net income; and to work always toward this ideal will develop the intelligence and accuracy of both the citizen and the tax lister — qualities greatly to be desired.

Shall this net income be taken for taxation in one lump sum? Shall it be put into separate classes, each according to their peculiar industrial nature? To put net income entirely in one lump sum is, from the administrator's point of view, very easy, but is very faulty from the point of view of the theory. Net incomes from various groups of production do not always bear the same relative importance to the life of the citizen, or that of the State. Some are of more value, others of less. To tax all net incomes under one class is to fail to differentiate between these differences, which are in reality very vital. But, when different classes of incomes are made, what shall be put into one

class, and what into another? It is just here that the idea of different classes of incomes finds its greatest difficulty, both in theory and in practice. Certainly not as yet has the principle of classification and of rate making per classes been defined. We have, to be sure, a more or less vague notion that one's income should be divided into classes, but exactly what shall be put into one class and exactly what into another we do not know. We have a vague notion that the rate upon the less permanent sources of income should be smaller than that upon the more permanent, but exactly how much less we have not the slightest idea. In fact, the problem is really as yet beyond the most daring theorist, to make well-defined classes of incomes and to prescribe a rate for each class. This theorist has already undertaken to place income from lands and houses in one class, income from government bonds in another, income from industrial bonds and stocks in another, income from industrial salaries and wages in another, and income from governmental employment in another. But how much greater shall be the rate upon incomes of one class than upon those of the other classes? This is the problem, and a most vital one, that is as yet wholly unsolved. Most probably income from the ownership of lands and houses is the most permanent, if we except income from government bonds, which in order to sell them at a fair price should not bear a heavy income tax, and should, therefore, in the main bear the heaviest rate. Those accruing from industrial bonds and stocks are, as we are well aware, oftentimes very fluctuating in amount, and consequently the rate upon them should be lower than that upon incomes from lands and houses. The income from wages and salaries in the industrial groups, like that accruing from the bonds and stocks of these groups, is more or less variable. And the permanent feature of governmental employment income is very slight, especially in a country like ours, where most of the office holders are of "but a few days and full of trouble." The tendency toward the lump sum income tax is, therefore, most strong; the theoretical and practical difficulties which arise from the different classes of the income tax are so many and great that we are almost forced to accept the less scientific but more easy form, — the same rate of taxation upon all incomes from whatever source. But still we should

strive to gain, as far as possible, the more correct and more just ideal, — taxes upon incomes according to the nature of their sources. How great the rate shall be upon each class of incomes, or upon the lump sum, depends, of course, upon the extent and intensity of the wants of the State, and as to whether the State resorts to a fairly high rate upon corporations, inheritances or land values.

Shall the rate of the income tax be proportional or progressive — that is, shall it be the same rate per hundred dollars of income irrespective of the number of hundreds, or a greater rate per hundred dollars as the number of hundreds of income increases? Over this question there has been an almost endless amount of talk, but, as I see it, we have come to no absolute agreement, if, indeed, to an approximate one. In theory there is much that is attractive in a progressive rate of taxation, but as to whether the attractive theoretical part is valid, we are in much doubt. The theoretical difference between the advocates of a proportional and a progressive rate is purely as to the method of reaching the basis of the ability of the citizen to pay taxes. They are in permanent agreement as to this point, — that ability to pay is the correct and just principle of taxation. The point of difference is this: Does a proportional rate justly and fully measure this ability, or does a progressive rate? The advocate of the proportional rate contends, and with much fairness it seems to me, that, when the State takes from the citizen say \$2 for every hundred dollars of income irrespective of its amount, it is placing an equal burden upon all its citizens. His position, from the point of view of a tax being a burden upon the citizen, or its payment being a sacrifice upon his part, is that the same rate per hundred dollars irrespective of the amount of income is an equal burden or sacrifice, and is consequently a fair test of the citizen's ability to pay for the support and development of his State. As opposed to such a view, the progressionist contends that two dollars per hundred taken from the income of a man who has but a thousand dollars is a heavier burden than two dollars per hundred taken from a man who has an income of two, three, four, five, or twenty thousand dollars. In order to reach the basis of equality of burden or sacrifice, of which he makes a great point, the progressionist demands that

the State levy a higher rate per hundred dollars of income as the income becomes higher in amount — say \$2 per hundred for an income of one hundred dollars, \$2.01 for an income of two hundred, \$2.02 for an income of three hundred, \$2.03 for an income of four hundred . . . \$2.09 for a thousand. Some such an increase in the rate as the amount of income increases, he thinks is demanded, whether we look at the citizen's ability to pay or the general benefits which accrue from the State to the citizen. He maintains that the citizen with a larger income receives more than a proportionally greater benefit from the State than does the citizen with a smaller income.

Just how much valid reasoning there is in such a view I am not prepared to say, though I am much inclined to doubt the chief point of such a contention. Apart from the fact that a progressive rate discourages the development of energy, thrift and foresight in the citizen, — his greatest and most valuable qualities both as a wealth maker and as a citizen, — apart from the fact that it is fundamentally a class proposition, a proposition of the lazy and the poor against the active and the rich, I am strongly inclined to doubt the validity of the purely abstract reasoning, to say nothing of the enormous administrative difficulties. In the first place I would contend that the citizen should, and in most cases does, render many other public services besides his taxation contribution to his State. In the case of the citizen who has but a small income, this extra public service is in the main exceedingly small, whether viewed directly or indirectly, even though we have a few illustrious exceptions. In the case of the man who has a large income, his extra public service is in the main much greater, even much more than proportionally greater. Now this extra public service must, if we act with fairness, be taken into our consideration of an income tax. As I conceive it, I am strongly inclined to believe that this extra public service is in the main sufficient to offset any progressive ability to pay which the citizen with a larger income possesses over the one with a smaller income.

And from the point of view of the administration of the tax the argument seems to me to be overwhelmingly in favor of the proportional rate, rather than a progressive one. How much shall the rate progress? This is a point which no man has

really and frankly attempted to discover. We have, to be sure, had statements — in fact many dogmatic statements — of how much the rate should progress with increasing income, but these statements are, as far as I am aware, entirely arbitrary, and consequently foolish. To discover just how progressive the ability to pay is in greater incomes and to establish just such a progressive rate is, to my mind, beyond the comprehension of man — certainly beyond that of the American tax legislator and tax lister. Even if we grant that the citizen with a larger income possesses more than a proportionally greater ability to pay and that consequently it is just for him to pay a more than a proportionally greater rate, and I do not willingly grant this much, the difficulty of determining the progressiveness of the rate is so overwhelmingly great, that I would not advocate its use, certainly not at the present and with our inefficient taxation machinery and officials.

My ideal is that the State shall regularly collect as much of its revenue as possible from taxes upon incomes and corporations, and that it may at times levy a small rate upon land values, in case this additional source of revenue is needed. The income tax, together with the corporation tax, which is in many respects an income tax, should now, I think, be the chief source of revenue for most of our States; their industrial conditions are now such that these two sources of public revenue, with, perhaps, a slight inheritance tax added, might well be made their chief, if not indeed their exclusive, sources.

But for the income tax to be justly levied and efficiently and honestly collected needs a radical change in the personal composition of our tax legislation makers and tax listers. Such a tax demands from its creators and administrators the maximum of intelligence, judgment and character — qualities which our present tax officials possess to the minimum degree. To put into operation a differentiated class income tax, and to cause its operation to be efficient and fair, it would be necessary for us to change, almost radically, our present taxation officials from those who prepare and pass the tax legislation to those who list the incomes. And to put such a tax into general operation, if it can possibly be done, either as the chief source of state revenue or as a very important source, would generally elevate the

intelligence and accuracy of bookkeeping of the citizen; and these certainly are traits which it is worth any people's serious attention to develop. It would now be greatly to their best interests to know exactly their net income by classes. Tax listing with such intelligent tax officials and citizens would be a matter of accuracy and fairness, instead of being a matter of inaccuracy, stupidity and dishonesty, as it now not infrequently is. For our States to continue to collect most of their revenue from that miscellaneous and unclassified thing called general property, a method of taxation which has no other defense except that based upon ignorance and stupidity, as many of them have in the past done and not a few still do, is to continue to place a great premium upon ignorance, stupidity, inaccuracy, laziness and dishonesty.

TAXATION OF THE PRODUCTS OF AGRICULTURE

BY N. J. BACHELDER

Master National Grange, Concord, N.H.

THE question of the taxation of farm products is so closely associated with the problem of the justice or feasibility of enforcing laws providing for the taxation of personal property, that it is necessary to take up the consideration of both subjects together. The primitive idea of taxation, that every form of property should be taxed equally, appears to be gradually giving way to the sounder view that taxes should be so levied as to yield the greatest amount of revenue with the least possible injury to productive industry. It is now beginning to be realized that the methods of taxation so long in vogue have been largely matters of guesswork, and that it is time that our systems of local and state taxation should be reformed and placed on a scientific basis.

Farm products should, in my judgment, be exempt from taxation. Such taxation imposes unnecessary burdens on both the producers and the consumers, and owing to the lack of uniformity in the laws and their enforcement in the different States, it places the farmers whose products are most heavily taxed at a disadvantage in competing with those whose taxes in this respect are the lightest, and to the extent that it adds to the price at which our farm products are sold abroad, it is a handicap on the American farmers in their contest, ever increasing in keenness, to hold their foreign markets against the competitive assaults of their foreign rivals.

I believe it is not disputed by any authorities on taxation that the tendency of taxing farm products is to increase their price, and to that extent to reduce their consumption. If this proposition can be maintained, it would of itself be a sufficient

reason for abandoning this form of taxation. The cost of farm products to the city consumer is to-day so abnormally high in comparison with the prices paid to the producer as to be a matter of such grave concern as to demand the immediate application of the necessary corrective measures. To continue a form of taxation which intensifies this condition, thus adding to the misery of the poverty-stricken masses of our great cities, and at the same time curtailing the farmers' markets, is not, it seems to me, sound public policy.

The lack of uniformity in regard to the taxation of farm products in the various States is another reason why such taxation should be abolished. If the farmers of a State in which these products are taxed are selling in competition with the farmers of other States in which no tax of this kind is imposed, the producer of the taxed articles is evidently at a disadvantage. While the difference may be small, it is still a handicap, and may often be the means of determining the production and sale of certain products.

The unsatisfactory nature of the tax on farm products is shown by the attempts in various sections of the country to minimize this tax by granting certain exemptions from it. How greatly conditions vary in the different States is shown by the following laws exempting from taxation farm properties of various kinds:

- ALABAMA:** All cotton and other agricultural crops grown in the preceding year; provisions and seed; \$25 worth of farming tools.
- ARKANSAS:** Statutes are so framed as to exempt growing crops from real estate assessment, although exemptions are prohibited by constitution.
- CALIFORNIA:** Constitution exempts growing crops; provides also that "cultivated and uncultivated land of the same quality and similarly situated shall be assessed at the same value." Constitution provides also (p. 12) that fruit and nut bearing trees under age of four years from time of planting and grapevines under age of three shall be exempt.

- CONNECTICUT:** Farm tools to the value of \$200 (this in addition to a general furniture and clothing exemption of \$500); swine to the value of \$50; poultry \$25; sheep, \$100 (cash, \$100); produce held by producer from preceding season, colts, calves and lambs; fuel and provisions for use of one family; tree plantations on lands not exceeding \$25 an acre, not less than 1200 trees to acre — when trees are grown to an average of six feet, exempt for twenty years.
- DELAWARE:** Farming utensils; grain and the produce of land; provisions necessary for the use and consumption of the owner for a year (not including live stock).
- IDAHO:** Growing crops; tools, household goods, farming implements and machinery to \$400, irrigating canals and ditches when used by owner on his land.
- IOWA:** Farm produce and wool of the harvest or shearing of the previous year; all poultry, ten stands of bees, all swine and sheep under six months and all other domestic animals under one year; farming utensils to \$300.
- KENTUCKY:** Crops grown in the year the assessment is made and in the hands of the producer.
- MAINE:** All poultry and eggs; produce in the hands of the producer; most live stock under six months; farming utensils.
- MARYLAND:** Crops in the hands of the producer; \$300 worth of farm implements.
- MASSACHUSETTS:** Farming utensils; certain tree plantations for ten years (also young live stock).
- MICHIGAN:** Certain young live stock.
- MISSISSIPPI:** Farm products and implements; and certain live stock.
- NEBRASKA:** Exempts "the increased value of lands by reason of line fences, and fruit and forest trees grown and cultivated thereon" (constitution).
- NEW HAMPSHIRE:** For ten years, improvements caused by reclaiming swamp lands; certain young live stock.

NEW YORK: Has a few small exemptions of furniture, implements, live stock, etc., being such property "as is exempt from execution."

PENNSYLVANIA: Has no general property tax; no state tax on farm products; locally taxes only "horses, mares, geldings and cattle above the age of four years."

RHODE ISLAND: Land not worth over \$25 an acre and planted with certain trees exempt for fifteen years after trees are four feet high.

TENNESSEE: Growing crops; the direct produce of the soil in the hands of the producer or his immediate vendee.

VERMONT: Farmers tools; family provisions for one year; poultry to \$20; certain young live stock; hay and produce to winter out the stock.

WASHINGTON: Fruit trees, not nursery stock, for four years after being transplanted in orchard form.

WEST VIRGINIA: Certain live stock.

WISCONSIN: Growing crops; provisions and fuel for six months.

Summarized, this shows that there are twenty-two States in which there are exemptions of crops, trees or live stock.

Four States exempt growing crops only. Four States exempt all produce in hands of producer — Tennessee extends this to "his immediate vendee." Three States exempt all produce for a year; and three states, all farm produce. Thus there are in all fourteen States which exempt crops from taxation. Two of these and two other States exempt fruit trees, making a total of sixteen States that encourage the growing of things by tax exemptions.

Five States exempt all farm utensils, and five States exempt farm utensils to a limited amount of from \$25 to \$400.

Ten States exempt young live stock, and two States exempt all poultry, and two States a limited amount. One State exempts eggs and one State ten stands of bees.

In the face of such diversity of practice it seems to me to be self-evident that a diffusion of tax knowledge sufficient to insure a uniformity of treatment in the taxation of farm prod-

ucts by the various States would be more than sufficient to insure the total abolition of such taxation.

The exemption of manufacturing establishments and manufacturing materials from taxation is very ably advocated by many of those who are students of the manufacturing side of the tax question, and while I hope that one of the results of this Conference will be that many of us will have clearer vision on this and many other phases of the tax problem, I only mention it here to say that every argument I have heard advanced or that I believe can be advanced, in favor of manufacturing or other industrial exemptions, can be used with increased force in favor of the entire exemption from taxation of agricultural products.

There is undoubtedly a strong trend toward the total exemption from taxation of all forms of personal property on the plea that from the very nature of the conditions it is impossible equitably to enforce such taxation. Whether this be true or not, it is certain that the burdens of the personal property-tax laws fall far more heavily on the rural communities than on the cities, and that under existing conditions the farmers in the majority of cases are compelled to pay more than their fair share of personal property taxes. An examination of the personal property-tax returns of the principal States shows that the amounts paid in personal property taxes by rural communities are outrageously excessive as compared with the amounts paid in personal property taxes by the cities.

Since farm products are a species of personal property, it follows that under the present methods of assessing personal property, and the notorious evasions of the large owners of intangible personal property in the cities, such farm products as are now subject to taxation are made to bear an excessive burden of taxation because of the increase in the tax rate necessary to provide the required revenue when such an enormous amount of other forms of personal property evades taxation entirely.

From whatever point of view the taxation of farm products is considered, the conclusion seems to me to be inevitable that such taxation has no redeeming features by which it can be justified; and I would most respectfully submit to this Conference for its consideration the proposition that the public welfare would be advanced by adopting generally some of the exemp-

tions of farm property now contained in the laws of the several States so that the following property should be exempted in all the States:

FIRST: All growing crops and all crops for a short period after harvesting.

SECOND: All animals raised for food purposes under a certain age.

THIRD: All farm work animals should be declared to be tools of industry and brought within the exemptions now granted to tools; and the value of tool exemptions should be expanded so as to include the value of such work animals.

These exemptions, operating on all alike, would benefit all the consumers of the country as well as farmers, thus including the entire population.

FOREST TAXATION

By A. C. SHAW

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THE efforts of the States to secure the reforestation of the denuded watersheds of their navigable streams and protect the farms along such streams from periodical and destructive floods has developed inquiries as to why land valuable mainly for timber growing is allowed to lie idle, and instead of contributing its proportionate share of wealth and its tribute of taxes has become a burden to the people and the States.

Although the price of lumber has advanced steadily for some years, the wealth produced by timber cutting and selling is taken away from the localities where it was amassed and invested elsewhere, and nowhere in reforesting denuded timber lands.

The legislatures of all of the States where such denuded areas exist are confronted with the cry, "Unfair taxation of the timber crop and inconsiderate and excessive overvaluation of timbered lands." It takes a generation of time to grow a timber crop. The grower must stand an unusual risk from fire and depredation, and must not expect any return from land or crop for many years. The growers of ordinary crops reap their returns in one year and of fruit crops in three or four years.

In many States growing crops are expressly exempted from taxation. In none is it practical to tax ordinary growing crops, and yet timber upon which the growers of other crops are dependent because of its conserving effect on the streams and because of its domestic uses is taxed annually by valuation with the land and often overtaxed because the value of young growth is not properly estimated by hasty assessments made upon imperfect knowledge.

So-called equal and uniform tax laws and the joint classification of land and timber seem to be the causes of the injustice

in taxing the timber crop. Under the former no consideration is given to the risks which are incident to, and the length of time which is necessary for, timber growing.

Private capital must destroy its timber because excessive tax laws make it impossible to consider a second crop. In many States land which is chiefly valuable for timber growing has been denuded and become waste, and now encumbers the delinquent tax lists or produces nothing and returns no tax. The joint classification of timber and land does not tend to secure a fair consideration of the timber, but does result in hasty and inexpert valuations which are most often excessive. Many States are striving to enact laws to promote timber growing and reforestation of denuded lands.

Special laws have been made in many, but few of them are practical. Some provide for bounties; others provide for exemption of land and timber for a term of years; and most of such laws seem intended to secure a growth of timber on lands which have never grown it or to introduce trees which are not indigenous to the respective localities.

The supreme courts of some of the States have declared that it is legal to depart from the common law classification of property and to declare that, for the purpose of taxation, growing timber shall be considered personal property and taxed separately from the land on which it grows. This action alone would tend to secure fair assessments by arousing intelligent consideration of both timber and land.

The constitutions of Colorado and Nebraska expressly provide that the increased value of private lands caused by the planting of trees thereon shall not be reckoned in fixing the taxes of such lands. California has a similar statute, which, however, only exempts fruit trees and grape vines grown for orchards and vineyards. These constitutional provisions do not, however, prevent denudation, since they refer only to planted areas. It would not be fair to relieve from all taxation land upon which timber grows, and it would not be fair to exempt matured timber on land suitable for agriculture. Such actions would unjustly increase the burdens of other land-owners and tend to prevent the best use of some of the land. No unfairness can, however, result in exempting, for a term of

years, growing and immature timber upon land chiefly valuable for timber growing. The following States permit reasonable exemptions: Connecticut, Delaware, Kansas, Maine, Maryland, Michigan, Mississippi, Missouri, New Jersey, Vermont and Wisconsin. Other States by their constitutions permit classification and confine the requirement of equal and uniform rate to the class in which property is placed. Because of the constantly decreasing timber supply and constantly increasing denudation of the watersheds with the resulting floods, disastrous alike to navigation and agriculture, there should be no delay in taking action to encourage timber growing whenever such action may be taken without injury to other interests.

In some States no relief can be secured except through amendment of their constitutions. Those States which by existing constitutions permit such encouragement are fortunate, since if they act promptly capital will be attracted to them, and they will be the first to make what is now worthless, denuded land a source of revenue and a means of livelihood to their citizens. A table has been prepared showing the States which may exempt, those which may classify and those which must amend their constitutions to secure relief in forest taxation, but since it has only local interest it is unnecessary to give it here.

GOVERNOR GUILD: Now, gentlemen, the meeting is open for criticism or discussion. What is your pleasure?

MR. JUDSON (Missouri): The last paper read suggests that sometimes changes may be effected through practical arrangements when not provided for by law. We have an illustration of that in my State in regard to the assessment of farm products. The date of assessment has been changed in our State from the first of September to the first of June. For a number of years the assessment date was the first of September; then a number of years ago it was changed back to the first of August, and a few years since it was placed on the first of June. Now, you can see the advantage of this date to the farmer. On the first of June, under our law, the lists are supposed to be made up. Every citizen returns his property as of the first of June. The practice and working of that law is to exempt farm products from taxation. On the first of June the farmer has no crops harvested and he simply is taxed on his land. When the next June comes around, his crops have all been disposed of, so he pays no taxes on farm products. The operation of the law, as you can well see, is peculiar, because on the first of June the lists are made up not for the tax bills of this year, but for next year. Thus our assessments in Missouri are now being made up as of the first of last June. Of course, the farmer returns nothing but his land and his live stock. No crops are in existence. The tax bills are made up this winter and are payable next summer, and thus the result so desired by the paper just read is practically secured without any exemption under the law. It illustrates how results may sometimes be accomplished outside of the law by a mere adjustment or arrangement of the assessment machinery. I have no doubt parallel cases to this one of ours exist in other Western States.

Another point occurs to me. A very interesting paper was read on the "Taxation of Incomes," that the tax of incomes, when left to be disclosed by voluntary listing by the taxpayer, may be open to the same objection in effect that the attempted taxation of intangible personalty is open to, and that is, that

we are compelled to the statement of the individual as to his own income, which he states or not, as he deems proper. Any form of taxation which involves the individual's own disclosures as to his taxable property involves a psychological question as well as an economic problem; it involves the question of how much temptation is necessary to lead a man to refrain from disclosing his taxable property. Now, if that is the practical effect, I should say that that problem or that question is psychological rather than economic, if it is to be counted in the consideration of taxation measures.

MR. FROST (Washington): The University I represent is that great university of which it has been said that fools will learn and none other. I might say that our State is not the one to which the sun extends its first greeting, but that the sun in making its good night to this great country of ours, imprints its good night kiss upon the highest sun-capped mountain peak of the State of Washington.

It has occurred to me, coming as we do from the wild and woolly West to sit at the feet of the learned East, that we are attaining more profit from the discussion of these papers than from the papers themselves, and I should like if more time could be given to the discussion of the matters and questions suggested in the papers read and in the addresses. I think we will get more profit by such a process.

Following the suggestion just made by the gentleman from Missouri, who has spoken of the paper read, I might say that in our State we consider growing crops upon the land as not to be taken into consideration at all. If the land were to be sold, the growing crops would pass to the buyer with the land. We do not consider that; the crops, growing crops upon the land, are not taken into consideration as an element of value in arriving at the valuation of the property.

There are several other matters that have been evolving and revolving in my mind, and one of those is the matter of the inheritance tax. We have a very successful inheritance tax in our State. It has occurred to the tax commission to suggest to our honest legislators that it will be a very wise plan to curtail the right of inheritance somewhat; that is, limiting the right of inheritance payable to collateral heirs of

the third degree and cutting off the right of inheritance beyond that. We have numerous large estates, large for a new country, I mean, in our State now, where there are terrific struggles on between the representatives of the State and the heirs of very remote relationships, heirs so remote that it is more than likely that the decedent had no knowledge of the existence even of such persons, and it seems to me it would be a very wise plan to limit the right of inheritance to those relatives who would have some natural or moral right to look to the decedent for some contribution for support. I think this is a question that is possibly worthy of great consideration. The question was asked Mr. Purdy last night, referring to his paper, if life insurance were a proper subject for imposition of the inheritance tax. At that time I felt like saying that life insurance is something entirely different from property that passes to the beneficiary. I think our courts have held that in order for any one to become a beneficiary in a life insurance policy, that one must have some beneficial interest in the life of the insured, and that creates a contractual relation between the beneficiary named in the policy and the insurance company. The life insurance passes directly to the beneficiary named, and does not pass through the probate court. It does not become a portion of the estate, nor is it liable for the debts of the decedent, consequently an inheritance tax, so called, could not be levied upon that class of property. Mr. Purdy, as I understood, rather took the other view last night, but I differ from him.

MR. PURDY (New York): I think the gentleman misunderstood me, perhaps. I only discussed really the question presented by a case where insurance money went to the estate of the beneficiary, because, as the gentleman very rightly says, the State properly could not, even if it would, interfere with the passing of the money directly to the beneficiary.

MR. FROST (Washington): I would like to add further that I agree heartily with the gentleman in his position upon the income tax. I think we will all agree that the income tax would be a correct measure of taxation; but I should also like to ask the gentleman to outline his plan of machinery to put that income tax into operation. I have thought about it a great deal; I have tried to plan out machinery for its operation,

and I have not been able to devise the first wheel of the machinery to put it into successful operation, and if any gentleman here has evolved any plan, I should greatly like to hear it.

I have enjoyed all the papers, and in a good many instances it rather occurs to me there is a certain element that perhaps is not taken into consideration, and that is the element of the human or personal equation. That must always be considered. We have in Washington possibly a unique experience. Our tax commission succeeded in persuading the last legislature to pass every measure recommended by the commission, and we succeeded in doing that by taking up each subject separately; I think we also succeeded in that for the reason that we recognized the fact that the medicine or the pill to be taken goes down very much more easily if it is sugar-coated, and we have taken that into consideration along with the questions of equity, justice and fairness in these propositions of taxation. We have to take all these things and look at them in the light of experience. We have to consider a reason among ourselves as to what the people will stand for; and if the people will stand for it, can we persuade the members of the legislature to stand for it?

I would like to hear more discussions along other lines. We could much benefit from the discussion of these subjects. I have told you what we are up against out in my State. We can devise very fine systems; we can do work and get together on propositions that we think will be very equitable and just; but we all realize that we may not be able to get the legislature to adopt any such recommendations or any measures of that kind at all. I would like to hear from some gentleman as to just how to fix up the dose.

MR. RIDDLE (Columbus, Ohio): I am an outsider. I asked a question last night about insurance, and as that question has been raised this afternoon, I do not care to interrupt any of the delegates, unless it is to state that that question was not asked to trap Mr. Purdy into making any statement he was not prepared to make.

GOVERNOR GUILD: I do not think any one understood that you asked the question in anything but perfect sincerity of purpose and good faith.

MR. RIDDLE (Columbus, Ohio): Thank you, sir. I asked the question for the reason that an inheritance passing through an insurance policy to the wife or child of the insured would be one means of escaping taxation. We understand it, a person may acquire property in real estate or any other form by direct purchase, or if not, a person living entirely upon the income of his wages may apply that entirely to insurance and could leave an estate much larger than he would ever be able to acquire through the purchase of land. It was upon that account that I asked the question. I am opposed to all forms of inheritance tax absolutely, from the highest inheritance down to the very smallest; if it is wrong for the smallest to be taxed, then it is wrong also for the largest. I wanted to put the proposition in that form so as to raise the question whether or not it would be a proper thing to do, in taxing insurance.

A DELEGATE (Massachusetts): I merely wish to say a word. After hearing the admirable paper read by Professor Bullock, I feel that this assembly agrees with it for the most part, that an inheritance tax, if imposed, should be for revenue and not for any literary purpose, and I want to make an appeal along that line for reasonable rates, and not only reasonable rates, but that the same rate should be adopted in all States. The rate should be uniform. The citizen of one State should not be made to pay 2 or 3 or 4 or 5 per cent on his property, while in another State he would be taxed only three fourths of 1 per cent or 1 per cent. You are cutting off the heads of your own citizens if you are doing that. I am going to confine my remarks entirely to direct inheritance; I want to bring before the convention, I want you to realize, that 1 per cent on direct inheritances has been adopted by a majority of the States of this country as a tax on inheritances. I wish to read to you the rates in a few of the States:

Connecticut	One half of 1 per cent
Illinois	1 per cent
Montana	1 per cent
Michigan	1 per cent
Nebraska	1 per cent
Wyoming	1 per cent
South Dakota	1 per cent

Washington	1 per cent
California	From 1 to 3 per cent
Colorado	2 per cent on direct inheritances
Louisiana	There is a 3 per cent tax, but that tax is for educational purposes by statute, and if the property has paid taxes there is no tax at all.
Massachusetts	1 to 2 per cent
Minnesota	Where they also have a sliding scale, it varies from 1½ per cent up to 5 per cent. In other words, the State of Minnesota has gone the majority of States five better on taxes.

A DELEGATE: Do they have any exemptions?

A DELEGATE (Massachusetts): Not the same as in the majority of other States.

A DELEGATE: That is a very vital point, it seems to me.

A DELEGATE (Massachusetts): I have a paper here which I shall be very glad to hand you. The exemptions in Minnesota are simply on the general scale given by all other States; I think \$10,000 is the common exemption.

North Carolina	Three fourths of 1 per cent
Wisconsin	1 to 3 per cent
Utah	5 per cent

Now again I appeal for the adoption of some simple rate like 1 per cent. I want to read a little clipping here that I wrote a year ago in the form of an editorial to show the excessive rates.

"The maximum rate on collateral inheritances are 15 per cent in California, North Carolina and Wisconsin; 12 per cent in Washington; 40 per cent in Louisiana, South Dakota and Utah; 7½ per cent in West Virginia; and 6 per cent in Colorado, Nebraska and Oregon. If a citizen of Utah should die, leaving to his widow or child shares of preferred stock in the Great Northern Railroad, representing roughly \$100,000 in value, it would be taxed 5 per cent in Utah, 5 per cent in Minnesota, besides whatever Congress might see fit to impose. If a citizen of California should die leaving a large block of Northern Pacific stock to a collateral heir, it would pay 15 per cent in California, and the same in Wisconsin, besides whatever the United States may eventually take of the 70 per cent of the market value of the stock still remaining."

These figures do not come nearly as high as some statistics show, but at the same time they illustrate the need of facing the situation, making the tax reasonable and equitable and uniform throughout the country.

That brings me to the further point, the attempt by States, which is almost universal, to try to reach the property of non-residents; that is, instead of leaving the taxation to the State having jurisdiction of the person, the State governing the general succession of the property, to levy an additional tax to that put on by the State having charge of the general succession. People in States where there is development going on want people in other States to come and buy the securities of those developing companies, and want their property, their capital and money to come out there and help that development. You say to them, — California, for instance, — “If you come here and take these securities, help us develop, take the stocks of these companies that are being developed, when you die, you are going to have to pay 10 or 15 per cent on that property.” We have a very strict and rigid law in Massachusetts to reach property, a new law passed this year. I have been told by several bankers lately that since that law was passed, the demand from outside for Massachusetts securities had decreased, and large blocks of Boston and Providence stock and other railroads had been sold by people outside of the State, because they said they would not have their estates pay inheritance taxes in two places. The same thing is true in New York as to General Electric stock, for example, that Massachusetts citizens have been selling those stocks because they objected to having their estates subjected to both taxes. Therefore, I appeal to this convention that in the resolutions there may be something in favor of a uniform inheritance tax, something that will be equitable, that people will not try to evade, but that will provide for one tax. I think that should be included, in fairness to all.

A DELEGATE (West Virginia): I merely wish to indorse what the preceding speaker has said. In asking whether there was any exemption, I had in mind my own State, where the State does exempt \$20,000 of property, and in Minnesota, I think, \$10,000, from the operation of the tax of 3 per cent.

I don't know whether 1 per cent or 3 per cent is the proper amount, or which is too high or which too low. I merely wished by asking the question to emphasize the point that you cannot take figures always as indicating the exact conditions, for in some States there is no exemption and in some States there is an exemption as high as \$20,000 or \$25,000, and it is fair to take those matters into consideration in the study of this question.

If you will pardon an "Indian," Mr. Chairman, referring to your allusion in introducing a professor of Harvard University, I would wish to take exception to one part of that professor's very able and interesting discussion, and I would further wish to commend much of it also to the prayerful consideration of Professor Roosevelt at Washington, because he told how so easily we could in one generation stop the building up of swollen fortunes by unlawful means, if we would just follow his advice, and that the inheritance tax would not be a remedial agency alone. I am inclined to agree with him in large part as to using the inheritance tax as a punitive measure for correcting the evils of wrongfully acquired or skillfully acquired swollen fortunes, but it seems to me that he traverses a pretty wide range of subjects other than the inheritance tax in his discussion, and that in proving that the inheritance tax will not cure the evil he introduces another subject, and in a very didactic as well as empirical way, stated how we could cure the trust evil by the application of laws in relation to tariff, something entirely extraneous, of course, to the subject in hand; to that extent at least, I would not wish, as one of these tariff Republicans, to remain silent. If the distinguished gentleman meant that we could cure the evils of great trust combinations now by lower tariff, I do not see his meaning quite.

GOVERNOR GUILD: The Chair must respectfully call the gentleman to order. I did not understand Professor Bullock to go into the tariff question at all.

A DELEGATE (West Virginia): I submit the question to the House, and if he did, that the Chairman did not call him to order for taking up matter not in discussion here. I do not recall the exact words, perhaps you will recall the sentence —

GOVERNOR GUILD: I must call the gentleman to order. That matter has no place in this discussion.

A DELEGATE (West Virginia): I just simply wished to call attention to it and I was practically through when the Chairman spoke. I was not going into the discussion of it further. I have plenty of opportunities for that in West Virginia.

GOVERNOR GUILD: The Chair is always delighted to discuss with the honorable gentleman from West Virginia any question. I particularly recall and am glad that when the Chair last spoke, in 1896, that the honored Governor was by no means through, but continued to hold office long after that time. (*Laughter.*)

MR. SUTRO (New York): It occurs to me with reference to the inheritance question, or the income tax, and the psychological features of it which were alluded to by one of the gentlemen in his discussion, that these matters are very much exaggerated. Certainly I think we will all admit that there can be no more wearing tax than the personal property tax, so far as the inequitable feature of the property tax is concerned. From conversations I have had with officers who are charged with the duty of collecting the income tax, before it was declared unconstitutional by the Supreme Court — at least with the duty of collecting the information with reference to the incomes, or the persons who made these returns, I have become convinced that the psychological feature is no more difficult in the way of arriving approximately at the true conditions of the income of persons, than it is to arrive at the status of the personal property of persons.

A DELEGATE: May I interrupt just a moment? One of the chief difficulties under our present system of taxation is the question of arriving at the value of personal property. We are unable — at least in our State — with any degree of accuracy or certainty at all to ascertain the personal holdings of a man. That is the objection to general property taxes as applied to personal property.

MR. SUTRO (New York): I fully agree with the gentleman. I am not discussing the question of the advisability or the desirability of continuing the present property tax. I am only suggesting that there would be no more difficulty, indeed, I

believe less difficulty, in obtaining accurate and correct returns with reference to the income, than with reference to obtaining what are the personal property holdings of a person, which is the general property tax in almost every State.

A DELEGATE: We are entirely unable to ascertain the personal property holdings in our State.

MR. SUTRO (New York): We have some difficulty, sir, in every State in the Union. In fact my own information is, from the investigations that I have made, that the returns are more than satisfactory with reference to the personal income than with reference to the value of personal property; but for other reasons and from another point of view, the income tax is, in my opinion, the fairest and justest tax that can possibly be levied, and I believe that that is the opinion of all the writers that I have read upon the subject of taxation.

Now, I must say that the papers of Professor Bullock and of Professor Raper made a great and deep impression upon me, and I think that they are both most admirable addresses. It is not the function of a State to regulate sociological conditions. I think that is an assertion that is in itself true. Certainly it has no such function when we are discussing questions of taxation. The purpose of a State in taxing whatever object or objects it may tax is to raise revenue to support the government, and if it goes beyond that, it goes beyond its function. If fortunes ought to be regulated or reduced by the imposition of a confiscatory tax, there is no more reason why, during the lifetime of such person who is a millionaire or a multimillionaire, his fortune should not be subjected to a higher rate of taxation than that of the poor man. If the purposes and objects of a graduated income tax are simply that, and I cannot conceive that it could be any other from the economist's point of view, then it is fallacy, because if immense fortunes should be curtailed and regulated, there is no reason that I can see for waiting until the person dies. In fact those fortunes are more apt to regulate themselves after death of such a person than during his lifetime. It is the history of large fortunes that after a number of generations they disappear, with very few exceptions; therefore I never could understand the logic of the theory that the income tax should be on a progressive scale. More-

over, it is un-American, it is unfair and unjust. Income taxes at a proportionate rate are progressive in themselves, and a man who has an immense fortune pays proportionately an immense tax in comparison with the man who has a very small fortune; therefore that regulates itself in that way. I am speaking of the inheritance tax, gentlemen, and the same thing holds true with reference to income. The man who has a large income necessarily pays in proportion to his income a very large income tax, without making it progressive, and I express again the same views I have before mentioned with reference to the unfairness and to the fact that it does not reach the result which was intended to be reached. This is true with reference to progressive inheritance and income taxes both. I am certainly impressed with the general views expressed by these two gentlemen, that inheritance and income taxes are proper objects for the government to take into consideration. The feature should be eliminated altogether that the object is to curtail fortunes or to rearrange our sociological conditions. You can only reach those swollen fortunes in the manner that Professor Bullock explained — reach the man now. Prosecute them in the courts and restore the funds which they may have acquired in an improper or unlawful manner to the place where they belong, but do not attempt to do that through the medium of taxation. (*Applause.*)

MR. BALDWIN (Massachusetts): As to the inheritance tax, many people, perhaps, look to the inheritance tax as an instrument for reaching these swollen fortunes. That taxation should be employed not merely as the agency for supporting the government, but as affecting the reorganization of society thereby. That theory, however, I conceive to be a most mischievous and harmful one, and the effect of the general adoption of that principle would be to promote extravagant expenditures and class legislation.

A DELEGATE (Connecticut): As regards the different practices in connection with the inheritance tax, the State of Connecticut has been guilty of adopting the double taxation in connection with the fact that she has taxed shares of stock and registered bonds held by the estates of non-resident decedents, where probably those same things are taxed in other

States, their own States. In trying to do better a law was passed which went into effect the first of September, and while Connecticut is not entirely innocent now, we shall exempt the shares of stock and registered bonds held by persons in States which cannot tax shares of stock and registered bonds of other corporations held by citizens of another State. In endeavoring to try to enforce this statute we have found it difficult to ascertain from the different States whether they would tax shares of stock and registered bonds of other corporations held by citizens of Connecticut, and so far the State of Connecticut is unable to say definitely whether they should or should not tax shares of stock and registered bonds of several States in the Union, and I trust that when the program is carried out as suggested by the gentlemen, that we have equality, and that such a difficulty will disappear.

FIFTH SESSION

WEDNESDAY EVENING, NOVEMBER 13, 1907, 7.30 TO 10 O'CLOCK

CHAIRMAN, GOVERNOR GUILD OF MASSACHUSETTS

PROGRAM

1. RATING ON UNIMPROVED VALUES IN NEW ZEALAND.
Professor James Edward Le Rossignol, Department of Economics, University of Denver, Denver, Colo., and William Downie Stewart, Dunedin, New Zealand.
2. THE SINGLE TAX.
C. B. Fillebrown, President of the Massachusetts Single Tax League, Boston, Mass.
3. THE TAXATION OF UNEARNED INCREMENT.
Professor H. J. Davenport, Department of Political Science, The University of Chicago, Chicago, Ill.
4. SOME GENERAL CONSIDERATIONS CONCERNING SOVEREIGNTY AND TAXATION.
Professor Lindley M. Keasbey, University of Texas, Austin, Tex.
5. THE TAXATION OF INTANGIBLE ASSETS IN TEXAS.
Professor Samuel Peterson, University of Texas, Austin, Tex.
6. MULTIPLE TAXATION AND TAXATION OF CREDITS.
W. G. Langworthy Taylor, Professor of Political Economy and Commerce, University of Nebraska, Lincoln, Neb.
7. TAXATION OF MONEYS AND CREDITS.
Frank G. Pierce, Secretary of the League of Iowa Municipalities, Marshalltown, Ia.
8. FARM MORTGAGES AND DOUBLE TAXATION IN VERMONT—SITUATION AND REMEDY.
Charles W. Mixter, Professor of Political Economy, University of Vermont, Burlington, Vt.
9. DISCUSSION.

RATING ON UNIMPROVED VALUES IN NEW ZEALAND

BY PROFESSOR J. E. LE ROSSIGNOL

Department of Economics, University of Denver, Denver, Colo.,
AND W. DOWNIE STEWART, Dunedin, New Zealand.

RATING on unimproved value should be clearly distinguished from the ordinary and graduated taxes on land levied by the general government, but a brief sketch of the latter system will help in the explanation of the former, for they are historically and logically connected with one another.

Prior to 1892 the revenues of the government, chiefly derived from duties on imports, were supplemented by a tax of one penny in the pound on all assessed real and personal property, with an exemption of £500 of the value of each assessment. In the year ending March 31, 1892, this tax yielded £356,741. Additional revenue was needed, there was agitation in favor of breaking up the large estates, and there were abuses connected with the general property tax; so that in the year 1891 "The Land and Income Assessment Act" was passed, abolishing the property tax and establishing in its place taxes on land and incomes.

From a fiscal point of view the new taxes were very successful, yielding in the year 1892-1893 the sum of £364,548, and in the year 1905-1906 the large amount of £647,572, of which the land taxes yielded £385,756. Of this amount the ordinary land tax yields about £281,000 and the graduated land tax £105,000.

It is worth noting that these taxes were established under the brief administration of Ballance, and continued during the long premiership of Seddon, the chief of the Liberal party, whose power rested largely upon the votes of the small farmers and the working people of the towns.

The Act of 1891 allowed deductions for improvements up to

£3000, but, by the amended Act of 1897, the value of all improvements was exempted from taxation. The consolidation Act of 1900 is now in force, with amendments made in 1903. The rate of the ordinary land tax is fixed by the annual taxing act. At present it is one penny in the pound on the unimproved value. The tax on mortgages is $\frac{1}{4}$ of a penny in the pound. An owner whose land is mortgaged is allowed to deduct the amount of the mortgage from his total assessment, but the full value of mortgages on land owing to him is added to his assessed valuation. If such net value is less than £1500 the owner pays no tax; if it is £1500 he pays on £1000, and there are diminishing exemptions up to £2500, beyond which there is no further exemption.

The graduated land tax begins with a tax of $\frac{1}{8}$ of a penny in the pound when the unimproved value in any assessment amounts to £5000, and increases by 16ths to a maximum of 8d. in the pound on estates whose unimproved value is £210,000 or more. Mortgages are not chargeable with graduated taxation, nor deductible in assessments. Non-resident owners pay an additional tax of 50 per cent on the amount of the graduated tax. A non-resident owning land of which the unimproved value was £210,000 would pay the ordinary tax of 1d. in the pound, a graduated tax of 3d., and an additional tax of $1\frac{1}{2}$ d., making a total of $5\frac{1}{2}$ d. in the pound, or 2.3 per cent of the unimproved value. An official return presented to the House during the session of 1906 showed that there were 63 rural estates of an unimproved value of £50,000 and upward, fourteen estates with an unimproved value of £100,000 and upward, one estate of 218,866 acres valued at £214,978, and one of 101,221 acres valued at £276,118. The capital value of the two largest estates was £214,978 and £276,118.

Because of the deductions and exemptions mentioned above the burden of the land tax falls altogether upon relatively large holders. In the year 1905-1906, out of 145,000 landholders only 24,246 paid any land tax at all, and of these one half paid less than £5.

The land tax, together with other legislation, and the natural tendency toward the division of large holdings, has had some effect in reducing the size of the great estates. In the year

1896-1897, 17.5 per cent of the holdings were of 320 acres and over, and 90 per cent of the total acreage was thus held, while in 1905-1906 such holdings were 20.6 per cent of the whole, and included 89 per cent of the total acreage. The great estates, however, show a relative decline in number and acreage. In 1896-1897 there were 501 holdings of 10,000 acres and over, containing 54 per cent of the total acreage, and in 1905-1906 there were 502 of such holdings, containing 47 per cent of the total acreage. In 1896-1897 there were 112 holdings of 50,000 acres and over, comprising 30 per cent of the total acreage, while in 1905-1906 there were 90 holdings of this class, comprising 24 per cent of the total acreage.

For a number of years the policy of the government has been directed toward the breaking up of the great estates. In the year 1892 the Cheviot estate of 84,755 acres was bought for £260,220, under "The Land and Income Assessment Act," and presently sold or leased to a large number of small holders. In the same year was passed the first of a series of Land for Settlements Acts, under which 938,173 acres have been bought by the government and leased in perpetuity to small holders. Many of these small holders have made large profits upon the land thus acquired, while the country has gained much from closer settlement and more intensive farming.

During the session of 1906 the government brought in a bill to limit the holdings in rural land of any individual or corporation to an unimproved value of £50,000. The bill met with strong opposition and was dropped, but in the present session another bill has been introduced, providing for a considerable increase in the progressive tax on lands of which the unimproved value is £40,000 and over.

Before the year 1896 there was no uniformity in the system of valuing land. The Land Tax Department periodically employed a small army of temporary valuers and each local authority had its own method of making up its roll for the levying of rates. But on October 17, 1896, was passed "The Government Valuation of Land Act," amended in 1900 and 1903, for the purpose of securing uniformity in valuation, particularly in the administration of the land tax and the rating on unimproved value.

The act provides for the appointment of a valuer-general and district valuers, to hold office during pleasure. The district valuers reside in their districts, soon become expert in their work and generally command the confidence of the people. There is little or no corruption or bribery. At first the valuation was about 10 per cent less than the true selling value, but presently much less, because of increase in land values. The valuation is not made at stated times, but is constantly being revised, although it is sometimes out of date. The officials state that there are no insuperable difficulties in the way of determining unimproved values and that the results are approximately correct.

The Act of 1896 defined *unimproved value* as "the difference between the total capital value of the whole property and the total capital value of all buildings and improvements," but the definition was found to be inadequate and the Amendment of 1900 gives a number of more elaborate definitions, thus:

"*Capital value of land* means the sum which the owner's estate or interest therein, if unincumbered by any mortgage or other charge thereon, might be expected to realize at the time of valuation if offered for sale on such reasonable terms and conditions as a *bond fide* seller might be expected to require."

"*Improvements on land* means all work actually done or material used thereon by the expenditure of capital or labor by any owner or occupier of the land, nevertheless in so far only as the effect of such work or material used is to increase the value of the land, and the benefit thereof is unexhausted at the time of valuation, but shall not include work done or material used on or for the benefit of land by the Crown or by any statutory public body, unless such work has been paid for by the contribution of the owner or occupier for that purpose: Provided that the payment of rates or taxes shall not be deemed to be a contribution within the meaning of this definition."

"*Land* means and includes all land, tenements and hereditaments, whether corporeal or incorporeal, in New Zealand, and all chattle or other interests therein, and all timber or flax growing or standing thereon: Provided that native bush or native trees which have been planted for shelter or ornamental purposes on an area not exceeding twenty-five acres shall not be included in the definition of land in this section."

"*Owner* means the person who, whether jointly or separately, is seised or possessed of or entitled to any estate or interest in land."

"*Unimproved value* of any piece of land means the sum which the owner's estate or interest therein, if unincumbered by any mortgage or other charge thereon, and if no improvements existed on that particular piece of land, might be expected to realize at the time of valuation if offered for sale on such reasonable terms and conditions as a *bond fide* seller might be expected to require."

"*Value of improvements* means the sum by which the improvements upon an owner's land increase its value: Provided that the value of improvements shall in no case be deemed to be more than the cost of such improvements estimated at the time of valuation, exclusive of the cost of repairs and maintenance."

The valuation of all the land and improvements in New Zealand was completed in 1898. The unimproved value was given as £84,401,244, and the value of improvements £54,190,103. In the year 1906 the unimproved value was £137,168,548 and the value of improvements £81,254,004.

"The Rating on Unimproved Value Act" of August 13, 1896, amended in 1900 and 1903, was a piece of legislation brought about largely by the influence of a few followers of Henry George, and was designed to give local governing bodies an opportunity of testing single-tax theories on a small scale. It was supported by the laboring class in general, who complained of high rents, and by many other persons in places where land was held for speculative purposes.

Before the passage of the act local rates were levied upon the capital value or the annual value of real estate, as determined by valuers appointed by the local authorities. The act provides for local option in taxation, in that counties, boroughs, town districts, road districts and other rating bodies may decide as to whether their rates shall be levied on the unimproved value, as determined by the government's valuation, or upon the annual or capital value of real estate as heretofore. A written demand, signed by from 15 per cent to 25 per cent of the ratepayers, according to the number of ratepayers on the rating district, must first be presented to the chairman of the district, requesting that the act be submitted to a vote of the

ratepayers, and the vote must be taken between twenty-one and twenty-eight days after delivery of the demand.

Under the original act it was necessary for at least one third of the ratepayers to vote, and a majority of their votes carried the proposal. Because of this provision the act failed to be carried in a number of districts, but now "The Local Government Voting Reform Act" of 1899 provides that a bare majority of the valid votes recorded is sufficient to adopt the act. If the act is adopted, no rescinding proposal can be submitted to the ratepayers until the expiration of at least three years, and if a rescinding proposal is carried, no adoption proposal may be submitted until after three years have elapsed.

Section 20 of the act reads as follows: "This act shall not apply to water rates, gas rates, electric-light rates, sewage rates or hospital and charitable-aid rates."

During the parliamentary session of 1905 a bill was introduced into the House by Mr. Henry George Ell to amend the principal act so as to permit the local authorities to levy "all or any of the rates mentioned in Section 20 upon the unimproved value." This proposal excited great opposition and a spirited debate, and the bill was lost. It shows, however, that the single-taxers of New Zealand are not satisfied with the small measure of land taxation which they have secured, and that they favor local option only as a means to an end, and, if possible, would make rating on unimproved value not optional but mandatory in every rating district in the colony.

Up to the 15th of May, 1899, the act had been submitted to the ratepayers in 23 districts, and in 21 cases received large majorities, the minorities in most cases being remarkably small. In eight cases less than a third of the ratepayers voted and the act was rejected, but in all of these districts it was carried at a later date. Up to March 31, 1906, the act had been rejected by 12 districts and adopted by 69, including 2 cities out of a total of 4, 19 counties out of 97, 38 boroughs out of 97, 9 road districts out of 214, and one town district out of 32. In the year 1904 the act was carried by 6 districts and rejected by one; in 1905 it was carried by 6 districts and rejected by 6. No district has ever rescinded the act, although three proposals to rescind have been made, and in 2 cases a strong opposition

was developed. In the third case the vote on both sides was less than when the act was carried. The vote is seldom a large proportion of the total ratepayers.

The indifference of many ratepayers to the rating of unimproved value is probably due chiefly to the fact that the rates in most districts are not a heavy burden upon the property holders. The general government supports the public schools and many charitable institutions, spends large sums of money on roads and other public works, bears the expense of valuation and even grants subsidies to the local bodies. The chief items of local expenditure are for roads, bridges, drainage, harbors, charitable aid and hospitals. Besides, over one half of the local revenues are derived from licenses, rents, governmental subsidies and other sources. In the year 1904-1905 the total revenue from rates in all the local bodies in New Zealand was £1,019,431. In the same year the total unimproved value was £122,937,126, so that the total rates were .83 of one per cent of the total unimproved value; and, if we suppose the valuation to be 80 per cent of the true value, the rates were only two thirds of one per cent of the true unimproved value. In counties and small boroughs the rates are very low, but in the larger towns they are much higher than the average. In Wellington they are 1.1 per cent of the unimproved valuation, in Christchurch 1.2 per cent, in Invercargill 1.8 per cent, in Devonport 1.7 per cent and in Stratford 2 per cent.

Early in the year 1906 the government made an investigation of the working of the act in all the districts where it had been adopted, and the report has recently been published as a Blue-book by the British government, but since the complete report was not accessible, the present writers made a similar investigation by means of a series of questions sent to the clerks of all the local bodies, 69 in number, that had adopted the act. Forty replies were received, of which 35 gave satisfactory answers. The questions and a summary of the replies are here given.

1. Has the system had any marked effect in discouraging the holding of land for speculative purposes? Yes, 12. No, 19. Indefinite, 4.

2. Has the system unduly forced people to part with land used for private gardens? Yes, 4. No, 22. Indefinite, 9.

3. Do you attribute to the system any alteration in the prosperity of your county, district or borough? Yes, 7. No, 22. Indefinite, 9.

4. Has the system caused any appreciable increase of buildings or other improvements? Yes, 12. No, 14. Indefinite, 9.

5. Has the system caused buildings to be erected in advance of requirements? Yes, 3. No, 32.

6. (a) Do you consider the system to work equitably? Yes, 19. No, 9.

(b) Do you know of any cases of hardship? If possible, give details. Yes, 14. No, 10.

7. Has it had any effect in (a) cheapening land, or (b) making it easier to get? (a) Yes, 5. No, 28. (b) Yes, 12. No, 22.

8. Do the ratepayers and public seem satisfied with the system? Yes, 22. No, 3. Indefinite, 10.

In further explanation of these questions and answers it should be noted:

1. The tax is too slight to have any marked effect in discouraging speculation, especially in view of the general rise in land values, but in a number of cases weak holders have been compelled to sell to stronger holders, or to buyers of small lots for building.

2. In a few places, as in Wellington, where there is a great scarcity of building sites, the tendency, already existing, toward overcrowding, has been increased. A higher tax would have a still greater effect in this direction.

3. The prosperity of New Zealand is chiefly due to the natural resources of the country, as yet only partially developed, and to the high prices for mutton, wool and dairy produce that have prevailed during the past ten years. The effects of the land legislation have therefore been obscured. The policy of the government in encouraging closer settlement has doubtless contributed to the development of the country, but the rating on unimproved value has probably had little, if any, effect in promoting or retarding general or local prosperity.

4. The increase of buildings and other improvements has been due chiefly, if not altogether, to the general prosperity of the country, and the consequent increase of population. Districts where the old system of rating has been retained have

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prospered as much as the others. From 1901 to 1906 the population of New Zealand, exclusive of Maoris, increased by 15 per cent. The cities of Wellington and Christchurch, where rating on unimproved value is in force, increased by 25 per cent and 18 per cent, respectively; while the city of Auckland, which has kept to the old system, increased by 22 per cent. Two of the suburbs of Auckland, Devonport and Grey Lynn, under the new rating, have increased by 35 per cent and 43 per cent, yet the more conservative suburbs of Remuera, Mount Albert and Epsom show gains of 42 per cent, 75 per cent, and 112 per cent. Karori and Onslow, suburbs of Wellington, which adopted rating on unimproved value in 1898 and 1901, have increased by 42 per cent and 82 per cent, while the suburban boroughs of Petone and Miramar, which did not adopt the new rating until 1905, have increased by 56 per cent and 95 per cent. The borough of Invercargill, which adopted the act in 1901, has increased by 16 per cent, and the borough of Invercargill South, under the old rating, has increased by 22 per cent. The boroughs of Waimate and Hamilton, where the new system has been in force since 1901, have increased by 20 per cent and 75 per cent, yet the boroughs of Timaru and Gisborne, with the old rating in force, show gains of 18 per cent and 108 per cent. The total population of the 21 boroughs which adopted the act before 1904 shows an increase of 24 per cent, while the total population of all the boroughs in New Zealand has increased by 22 per cent. The total population of the 10 counties where the act was adopted before 1904 has increased by 10 per cent, and the total county population of New Zealand has also increased 10 per cent in the same time. So there is no evidence to show that the rating on unimproved value has either advanced or retarded the growth of the districts in which it has been adopted.

5. The tax is not sufficient to stimulate building to any marked extent, but if it were, and a large number of people improved their land, for the sake of securing some revenue, and not in response to increased demand, rents in general would fall, and the owners of improved property would lose as much as they had gained by exemption from taxation, or more. At the same time the propertyless class would gain by the reduction of rents.

6. The question of equity in the majority of cases has resolved itself into a question of the interests of the several classes concerned. There are two classes of owners, those whose unimproved value is greater than the value of their improvements, and those who own a greater value in improvements than in land. Owners of the latter class are well satisfied with the rating on unimproved value, since it has reduced their taxes. Owners of the former class complain when their taxes are materially increased, but since land values have risen almost everywhere, most of these people have lost nothing and feel no great burden unless they are holding large quantities of unimproved land. There are many individual cases of hardship, as where a poor person in a borough has a large vegetable garden or a paddock for a cow. Some industries, too, such as lumber yards, foundries and dairies, situated within a borough, have had their taxes greatly increased, and have been compelled to move to the country, where land is cheap. Not infrequently people owning large houses built upon small lots have had their taxes reduced, while some of their poorer neighbors have paid more, but as a rule a large house is built upon a large piece of land and a small house upon a small allotment. Besides, rich people as a rule own more unimproved land than poor people. Therefore the adoption of the new system involves a shifting of the burden of local taxation from the many to the relatively few, and those few, in a progressive community, are usually those best able to bear it. In a stationary or declining community the case might be quite different.

Where the system had been adopted in counties containing towns, the taxes on rural property are relatively increased and those of town property relatively decreased, so that the country people complain, and demand a system of differential rating, or a separation of the towns from the rural districts for purposes of rating. Again, in rural districts the rates fall more heavily upon the holdings of new settlers than upon the improved holdings of their more prosperous neighbors.

7. Land values have risen greatly, notwithstanding the tax. This, together with the slight amount of the tax, is probably the cause of the general indifference of the ratepayers to the

question. There is still a great deal of speculation in land, and land values are probably too high, in view of a possible and even probable fall in prices of mutton and wool because of increasing competition on the part of Australia and Argentina.

8. A majority of the ratepayers have had their rates reduced and are well satisfied with this result. A large proportion of the minority are indifferent. The laboring class, who are interested in the question of lower rents, are largely in favor of rating on unimproved value, but only those who own real estate can vote on the question. Town clerks are inclined to favor the system because it permits of a simplified system of bookkeeping. The minority who suffer hardship from the new rating have not sufficient influence to cause it to be abolished.

The writers are aware of the fact that many people in New Zealand, particularly the followers of Henry George, give a glowing account of the success of rating on unimproved value, wherever tried. The Hon. George Fowlds, Minister of Education, holds that the land taxes are largely responsible for the prosperity of the country during the past ten years. Mr. Henry George Ell, M.H.R., is strongly in favor of the new system, and would have water rates, gas rates and all other municipal rates levied upon the unimproved value. Mr. George Laurenson, M.H.R., said in the debate already mentioned: "I can assure you that the rating on unimproved values system will yet be adopted by every municipality in New Zealand. In the next ten years it will be adopted in connection with every class of rate that may be levied in this Colony."

An official report to the government from the Land and Income Tax Department, summarizing the results of the investigation above mentioned, reads as follows:

"The effect has been to greatly stimulate the building trade. It has been the direct cause of much valuable suburban land being cut up and placed upon the market, and of the subdivision of large estates in the country, resulting in closer settlement. The effect on urban and suburban land has been very marked. It has compelled owners of these to build, or sell to those who

THE SINGLE TAX

By C. B. FILLEBROWN

President of the Massachusetts Single Tax League, Boston, Mass.

For the practical views which it is my privilege to present to this distinguished Conference I beg to assume responsibility individually, rather than as representing any organized body, who thereby might be compromised. To express my conviction in ecclesiastical form I begin with the "Credo."

1. I believe in the Single Tax defined by Henry George in "Progress and Poverty" as "The abolition of all taxes save those on land values," to be accomplished, as he said at Saratoga, "by the slow process of educating men to demand it"; to which he added, "In thinking of details it should be remembered that we cannot get to the Single Tax at one leap, but only by gradual steps, which will bring experience to the settlement of details."

2. I believe that the amount of the Single Tax should be limited to the needs of the State for an effective and economical administration of government. "It is a question of applying land values to common use, as far as they will go, or as much of them as may be needed, as the case may prove to be."

3. I believe in the classification formulated by the New York Ford Franchise Act, of a public franchise as "land," and a public franchise value as "land value," together with the plainly consequent converse truth, viz., that the site value of land is a private franchise value, because land depends for its value upon exactly those same concrete and tangible things which give value to a public franchise.

4. I believe with Henry George that "in truth the right to the use of land is not a joint or common right, but an equal right: the joint or common right is to rent, in the economic sense of the term. Therefore it is not necessary for the State to take land; it is only necessary for it to take rent." Accordingly,

I believe that a man who owns land owns the site, and every right and privilege, fee, title, etc., pertaining to the land, from zenith to earth's center, exclusive and absolute, as against any other individual, but nevertheless subject always to the right of eminent domain, and to the claims of the community to its share in the value of those rights and privileges, through the sovereign power of taxation.

The argument in the case may be put briefly as follows:

The three economic legs necessary and sufficient whereupon the Single Tax stool may firmly stand are found in three generic peculiarities quite exceptional in their nature, which distinguish land from houses or other man-made products. The failure to recognize this distinction is, we believe, sufficient to account for the crookedness of present systems of taxation. Such a recognition must lie at the very foundation of any just system of the future.

These three attributes, firmly grounded in orthodox economics, are, in economic language, as follows:

- A. The site value of land is a social product.
- B. A land tax cannot be "shifted."
- C. The selling value of land is an untaxed value.

These three fundamentals are worthy of brief separate consideration.

A. First in order is the fact that land value is a social product, i.e. it is created principally by the community through its activities, industries and expenditures. The value of land is based primarily upon economic rent, defined as "what land is worth for use," what it would command in the open market.

Strictly speaking this "worth for use" usually attaches not to the land itself, not to the earth's surface, not to the inherent capabilities of the soil, not to light and air or other bounties of nature resident in the land, but to scores of things exterior to the land and through it made available for use, so that, as applied to urban land, the following would be a more accurate definition:

Ground rent is the annual value of the exclusive use and control of a given area of land involving the enjoyment of those "rights and privileges thereto pertaining" which are stipulated in every title deed, and which, enumerated specifically, are as

follows: right and ease of access to water, health inspection, sewerage, fire protection, police, schools, libraries, museums, parks, playgrounds, steam and electric railway service, gas and electric lighting, telegraph and telephone service, subways, ferries, churches, public schools, private schools, colleges, universities, public buildings — utilities which depend for their efficiency and economy on the character of the government; which collectively constitute the economic and social advantages of the land; and which are due to the presence and activity of population, and are inseparable therefrom, including the benefit of proximity to and command of facilities for commerce and communication with the world — an artificial value created primarily through public expenditure of taxes. In practice, the term "land" is erroneously made to include destructible elements which require constant replenishment; but these form no part of this economic advantage of situation or site value.

Consequently ground rent may be said to result from at least three distinct causes, all of which are connected with aggregated social, as distinguished from individual, activity: (1) Public Expenditure. (2) Quasi-Public Expenditure. (3) Private Expenditure. Thus their very nature and origin would seem to point to land values as peculiarly fitted to bear justly the burden of taxation.

B. Second in order is the fundamental fact that a tax upon ground rent cannot be shifted upon the tenant in increased rent. The argument in the case may run thus: Ground rent, "what land is worth for use," is determined, not by taxation, but by demand. Ground rent is the gross income, what the user pays for the use of land; a tax is a charge upon this income, similar in its nature to the incumbrance of mortgage interest. It is a matter of everyday knowledge that even though land be mortgaged nearly to its full value, no owner would think to rid himself of the mortgage interest that he has to pay through raising his tenant's rent by a corresponding amount. Mortgage interest is a lien upon land held by an individual; similarly, a tax may be conceived most clearly as a lien upon land held by the State. Both affect the relations between owner and mortgagor, and between owner and State respectively; neither has any bearing upon the relations between owner and tenant. "Tax" is simply the name of that

part of the gross ground rent which is taken by the State in taxation, the other part going to the owner; the ratio these two parts bear to one another has no effect upon the gross rent figure, which is always the sum of these two parts, viz., the net rent plus the tax. The greater the tax the smaller the net rent to the owner, and *vice versa*. Ground rent is, as a rule, "all the traffic will bear"; that is, the owner gets all he can for use of his land, whether the tax be light or heavy. Putting more tax upon land will not make it worth any more for use. If the market value of a lot of land for use is \$300 a year, a tax of \$100 will not make it worth \$400 a year.

These two propositions (*A*) that land value is a social product, and (*B*) that a tax upon land cannot be shifted by the owner upon his tenant in increased rent, are well settled in the professional mind.

C. Third and last is the fact, a necessary corollary of the second, that the selling value of land is an untaxed value, a proposition which has received the specific approval of upwards of fifty leading American teachers of political economy, and has been seriously questioned by but two or three of the three hundred to whom it has been submitted.

Every purchaser of a piece of property knows, without argument, that he is governed as to the price he will pay, not by the gross income, but by the net income that will remain to him after all charges and incumbrances by way of mortgage or tax have been discharged.

To illustrate: assuming a piece of land worth \$300 a year for use to be free of all charges and incumbrances, and assuming the current rate of interest to be five per cent per annum, a purchaser would buy the lot for \$6000, because interest upon that sum would amount to the stipulated \$300 a year. But, assume that, on the contrary, it is found to be subject to a mortgage of \$2000, upon which the annual interest charge is \$100, then he will buy the land, not at \$6000, but at \$4000, the value of the equity remaining after mortgage interest has been paid.

But, assume further that this lot of land, besides being subject to a mortgage of \$2000, is subject also to an established tax of \$100, which charge the purchaser must also assume. He

will then purchase the land not at \$4000, but at \$2000. The tax charge of \$100 and the mortgage interest charge of \$100 each reduces the selling price of land by the same amount, \$2000. The mortgage and the tax together therefore reduce it by \$4000; and the purchaser will buy the land at \$2000, the value of the equity which remains after both mortgage interest and tax have been paid. This \$2000 is the capitalization of the annual value of the lot after all charges have been met. The gross value is the taxed value. The net value is an untaxed value.

It follows from the above too brief analysis that under the present system, *the selling value of land is an untaxed value*, and landowners who invest to-day are entirely exempt from taxation.

As this exemption of the present owner holds true to-day, so it will be true in future of each new purchaser subsequently to the imposition of any new tax. It is in the very nature of things that the burden of a land tax cannot be made to survive a change of ownership.

But when we turn to the case of the taxation of houses we find that no parallel appears. Whereas a tax upon the lot could not, in the nature of things, increase its annual rental or cost for use, a similar tax upon the house is added directly to the annual cost to the user. If a house costing \$6000 to build is subject to a tax of \$100, this amount must be paid annually in addition to an interest charge of \$300. Increasing or decreasing taxation upon the lot has no influence upon its annual cost to the user; while increasing or decreasing the tax upon the house increases or decreases in exact proportion the annual cost to the user. The moral of this illustration is that a tenant gets for use annually \$300 worth of land for \$300, and a house costing \$300 for \$400. In other words, a house tax of \$100 takes in taxation \$100 a year of the user's income. A land tax of \$100 takes in taxation no part of the income of the present owner, provided that he purchased the land after the tax was imposed.

The beauty of this illustration is that while land stands for everything except the products of labor, a house is here made to stand as the representative of any and all products

of individual labor, and the illustration thus becomes all inclusive.

The practical exemption of the selling value of land is vital in its bearing upon any proposition for obtaining an increased revenue from that source, while substituting the gradual exemption of other property.

In the light of the foregoing argument it is interesting to consider what the city of Boston might have done.

The following estimate indicates the gigantic proportions of the factor, ground rent, and its sufficiency to meet all reasonable costs of government, economically administered, not only without impoverishing the landowner, but without subjecting him at any time to a tax more burdensome or more continuous than that borne by every man that has lived in a house since a house tax was invented.

The gross ground rent of the land of the city of Boston is by careful estimate not less than . . .	\$50,000,000
Of this amount there is already taken in taxation . . .	10,000,000
Leaving to the landowners of to-day a net ground rent of	<hr/> \$40,000,000

The fact that this sum amounts to \$68 per capita, or \$340 per family, will help the mind to grasp its magnitude as a factor in the distribution of wealth.

State and local taxes upon improvements, buildings, personal property and polls amount to something over another	<hr/> 10,000,000
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If this additional amount were taken from rent there would still remain to the landowners a balance of	\$30,000,000
\$51 per capita, or \$255 per family	

Coming to the consideration of means by which more revenue may be gradually raised from the land and the burden of taxation made more proportionate and reasonable, choice may be had from a variety of methods. The one most frequently suggested is that of appropriating by taxation part or all of the future increase in land values. If Boston should decide

to start to-day and take in taxation her future unearned increment above the present value of \$635,000,000, the case would be exactly the same as that of some new community where no value has accrued, a situation in which the ideal justice of the single tax is so frequently conceded.

If Boston had decided ten years ago upon the large annual increase of one dollar per thousand each year for ten years in the rate of taxation upon its land, coupled with similar reduction in rate upon buildings and personal property, that city would be raising to-day from its land \$10 per thousand more than it does now, or,

Land \$635,000,000, at \$10, an increase of more than	\$6,000,000
The increase in land value in the same ten years was \$188,000,000, 5 per cent of which is over	9,000,000

And Boston would be taking in increased taxation to-day only two thirds of its land increment for the same ten years.

Under this supposition the \$447,000,000 valuation of ten years ago would still remain untouched by taxation, as is now the case with substantially the whole \$635,000,000 valuation of 1906.

The foregoing Boston figures are submitted simply for purposes of illustration, not in any way as support of a specific recommendation.

If the preceding argument is valid, it establishes the fact of gross inequality in the incidence of taxation as between land values and improvement values. If it is admittedly wrong that present land values should be untaxed, how can such fiscal wrong best be righted? Begin at once a transfer of taxes from improvements to land, so gradual that two old injustices will cease for every new one that is begun, until this untaxed value is made to bear at least its proportionate burden at the same rate with other things.

In conclusion I wish to emphasize this basic fact: that the burden of a land tax cannot be made to survive a change of

ownership has in turn this corollary of its own, viz., — that a new tax burden if imposed to-day would in one generation, by sale or by inheritance, cease to be a burden. If all taxes are finally collected from the landowner he will then be the only man taxed. If another generation serves to let his successor out from under the burden who will remain under it? Ground rent, economic rent, being an equivalent for value received, is not a burden, and if all taxes are ultimately taken from rent, it follows that in the course of two or three generations taxation may cease entirely from being a burden upon any one.

If professional economists and taxation experts will at once, to use a nautical phrase, quit their dead reckoning and steer their craft by the single tax pole star, time and tide will do the rest.

THE TAXATION OF UNEARNED INCREMENT

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PRECISELY because this paper — so far as it concerns itself with the single tax at all — will be devoted in about equal parts to criticism of the single tax program and to criticism of its critics, there will perhaps come some thread of intelligibility to this discussion if, at the outset, I make partial confession of my own convictions.

I believe, then, that there is a great and important truth at the heart of the single tax doctrine; that much has been lost and irretrievably lost by the centuries of delay in the recognition and the application of this principle; that the offered refutations are mostly erroneous or beside the point, — in about the same degree, indeed, as most of the arguments in favor of it, — both resting in theory upon substantially the same pre-suppositions. But I am unable to ascribe to the single tax program anything approaching primacy of importance as a method of social amelioration, and I am positive that its basis of theory requires a searching reëxamination and its practical program a radical reformulation, before anything enduringly good can be derived from the essential truth which it contains.

The following propositions are therefore submitted:

1. The social appropriation of the unearned increment of land values must be worked out not by a tax upon the capitalized present worth of the rental income but by direct process against the rental income. Not so much in general purpose and in general principle as in theory and in method is the single tax program defective.

2. But even so the principle is practicable only as applied to location rents. To burden the fertility must work the progressive exhaustion of this fertility. Only the irremovable

bases of value can safely be burdened — and this only upon the condition that the position rent be kept strictly separate from the fertility rent. Otherwise, the owner will, by the “skinning” process, deteriorate the property to the utmost possible extent, with the purpose of transferring his value investment into an untaxed form.

3. But subject to this limitation, — applied, that is to say, to the position rents of agricultural land and of town property, — the claim of society to all future increments should forthwith be asserted.

4. Rightly understood, the single tax doctrine is not a tax doctrine at all; it merely urges the employment of the tax machinery and administration for the appropriation of socially produced values.

5. It is, therefore, irrelevant to urge as an objection to the plan that it does not apportion public burdens to faculty, or that it burdens some classes more heavily than others, or that the derived revenues will not suffice for public needs. Nor is the advocacy of a general confiscation of existing land values any necessary or essential part of the theoretical case.

6. The principle of the proposed reform is especially important with reference to the unearned increments of public utility undertakings — transportation or other — and to all industries gravitating toward monopoly organization. But here also the method of percentage tax upon values is inappropriate.

7. Any delay or uncertainty as to the treatment of these unearned increments works out either in irreparable loss to society, or in gross injustice to individuals; at the same time it renders fundamentally unstable not only the entire fabric of stock values, but the superstructure of banking credit as well.

There are certain issues that need not long detain us. It was pointed out by General Walker more than two decades ago that of the three influences asserted by Henry George to be constantly making for the increase of land rent, (1) increasing population, (2) improving agricultural technique, and (3) developing facilities of transportation — only the first actually works in the direction ascribed to it; the second and third influences have precisely the opposite bearing.

But that the first point is admittedly valid suffices to establish the case, only that it is a less serious case. Three witnesses are not necessary to your suit, if only the testimony of your first witness is decisive. And surely the relation of expanding population to rent is disquieting enough. The law of diminishing returns applies here to signify that with an increasing number of human beings — other things being equal — a smaller per capita output of land products must obtain; and the law of rent thereupon asserts that, out of this diminishing aggregate of product, a constantly larger and larger share must accrue to the landholding class. Thus all the other classes suffer by a compounded pressure of adversity — the law of diminishing returns smites them with both edges of its sword: landowners are gaining through the progressive misfortune of society as a whole.

Taking all this to be true, however, it is obvious that the single tax principle promises no help for the lower level of productiveness attendant upon the crowding of population; only such amelioration is possible as is implied in a better distribution of whatever product there is to be distributed. The single tax method of achieving this better distribution is to use these increasing land rents in place of ordinary taxes.

The offered remedy, then, for whatever it is worth, must be found in some method of socializing these rental incomes. But whether the application of the plan should be purely preventive in character, as referring solely to future increments, or should rather be made to apply, *nunc pro tunc*, to such increments as have already accrued, is rather a problem of morals or of legislation than purely of economics.

Single tax discussion proceeds for the most part upon the assumption that the tax once imposed upon the landlord cannot shift. Should it shift this would precisely defeat the principle and purpose of the single tax; it would not attach ultimately to the unearned increment. On the other hand, the shifting of the tax would avoid the most bitter of the criticism. Taking the case to be one of a more indirect tax, a silence must fall upon all claims of radical amelioration and upon all charges of confiscation or of serious class injustice; regarded as a shifting tax, nothing remains of the issue.

What, then, is the incidence?

The argument according to which the landlord pays the tax is familiar enough. No tax can shift excepting as somehow disturbing the market values of products; all problems of incidence are value problems. Disturbance of market value is possible only through modifying either the demand for the product under consideration or the supply of it. It is, then, clear enough that a tax of the sort proposed can have no appreciable effect to modify the demand for agricultural products. And on the supply side also the solution seems almost equally clear; the tax, as only a portion of the rent, at no matter how high a percentage, can have no effect to drive out of cultivation either rent-paying land or marginal land. The principle that a half loaf is better than no bread applies to retain all supra-marginal land in its established use; and marginal lands can readily bear any possible percentage of tax upon their rentals, since they pay no rent. So long as the tax burden does not exceed the rent, no lands will be abandoned because of the tax.

Both demand and supply, then, remaining unaffected by the tax, it follows that prices must be unchanged; the incidence, that is to say, is not upon the consumers.

As between landlord and tenant the case is even clearer. Tenants can get no more for their products; they can pay no higher rents for their holdings; and the landlords, who have all the while been imposing all the rents they were able, have now no new leverage whereby to force an increase.

Superficially viewed the entire problem appears, therefore, to fall within that widest and most fruitful of generalizations in the theory of taxation, viz., that no tax upon either a producer's or a consumer's differential can ever be shifted; shifting occurs through supply influences only when marginal cost is increased.

That this is the traditional and accepted analysis of the case, and that in the main it is held in common by both the partisans and the opponents of the single tax, will hardly be disputed; the following citations of doctrine are typical. Bastable writes, "That on the hypothesis of perfect competition, a tax on rent must remain on the payer is an undisputed truth" ("Public Finance," p. 379). The reasoning appears, indeed, to be a

necessary deduction from the Ricardian theory of rent, and is bound up with the traditional distinction between land instruments and capital instruments in their relations to costs and to value. For, as Bastable insists, the case is quite other with capital: "Unlike land, it can be indefinitely increased by human foresight and prudence, having as a chief inducement the return to be obtained by investment. Taxation on interest . . . is therefore a direct discouragement to saving."

And Carver writes:

"All goods excepting land 'are perishable and reproducible while land is not' . . . These distinctions are important because important conclusions as to public policy depend upon them. . . . A tax on land . . . has a different effect from a tax on an article which is being produced, worn out, and reproduced by human effort. A tax on the latter class of articles has the effect of discouraging that effort and, consequently, of reducing the supply, whereas a tax on land does not affect the supply in the same way nor to the same degree." ("Distribution of Wealth," p. 129.)

The principle on which all this goes need not, then, be mistaken. A tax on any manufactured article will mostly shift to the consumer by raising the cost of it, and so reducing the supply of it, and thus enhancing the price of it; so a tax on any industrial appliance mainly or exclusively used in any line of production, or a relatively high tax on the capital employed in any line of production, must shift to consumers, since to the degree that consumers cannot be made to stand the tax, there must forthwith begin an outflow of the capital toward other and less burdened industries, thereby a restricting of the supply of the commodity in question and a lifting of the price upon such volume of the product as still comes to the market,—so far as persisting consumers are concerned the tax is a shifting tax. And even if the capital investment be embodied in specialized appliances, the shifting is none the less certain, but only slower — as taking place by the process of wearout and deprivation of upkeep.

But evidently, if the burden of taxation is equally heavy in every other direction of investment or of utilization, the shifting cannot occur; it is only changes in relative cost that are relevant to value.

Now note that whether the proposed land tax were alone adequate for the public necessities, — whether, that is, it really justified its title of “single tax,” — the plan must contemplate an exceptionally high rate of burden upon ground holdings. If, then, the burden is not slowly or rapidly to shift, this must be for the reason that the value investment cannot, either slowly or rapidly — by wearout or by any other method — be withdrawn or transferred.

But nothing is simpler than to wear out a farm. To crop and to withhold upkeep of fertility — the process called “skinning” — is a well-recognized way of marketing a land value; it is as easy as selling out to an insurance company by burning one’s property. Rural New England in its approximate entirety stands witness to this fact; tenant farming everywhere is its illustration; the progressive exhaustion of our continental heritage of fertility is a direful example; stupid or improvident farming — even without the stimulus of a stupid application of the stupid general property tax principle — must turn over to posterity an exhausted farm area.

It follows, then, that the general principle of the land tax is applicable for position values only. And, moreover, it is valid for these, whether rural or urban, only upon the assumption that the position rent is kept rigidly distinct, both in appraisal and in assessment, from the fertility of the improvement rent. So long as, through the misuse of a property, there is made possible the withdrawal of value from it, with a resulting lower appraisal and a lower burden, so long will the owner find bad husbandry to be good business, and so long will the redistribution of his fund of value investment appeal to him as his wisest pecuniary policy.

But I now insist that, subject to the foregoing limitations, the single tax advocates have a theoretically valid principle.

Let us see what there is in the commonly urged objections:

1. That the tax will not be sufficiently productive to cover the budgetary requirement; it is thus not a single tax.

This must be admitted as a valid objection so far as it attaches only to the propriety of the name; but it is only so far valid. There are, indeed, as we shall shortly see, still other and more weighty grounds of objection to the *name*.

2. That the tax is inelastic.

But this objection is valid only upon the assumption that the foregoing objection is not valid; it is not serious that one tax out of an entire system should be wanting in elasticity.

3. That there are many other unearned increments equally serious; why single out this one?

But not all are equally practicable of appropriation, and, in any case, that all ought to be appropriated is a passably poor reason for refusing to appropriate any.

4. That there are unearned decrements; is society to attempt to make these good?

But when once the entire position value has come to belong to the State, there can be nothing of it either to rise or to fall. It is no slight merit of the proposed system that speculation and boom and collapse, as dependent on land speculation, can no longer have place.

5. That it is disastrous in a democracy to have one class of society paying all the taxes.

This, again, is in conflict with the objection that the one source of revenue must prove inadequate. But the objection can best be discussed in connection with a further objection, namely:

6. That the tax is not proportional to faculty.

But, as has already been intimated, the tenability of the proposed measure is not safely to be rested upon the accuracy or the appropriateness of its name; there is, indeed, a more serious objection to the term "single tax" than the mere word "single"; the single tax is really not a tax at all, but an attempt on the part of society to collect for its own benefit the rentals upon the estates asserted to belong to it. No burden is menaced upon wages or interest or profits; instead there is proposed the appropriation of another, the fourth distributive share. True, it is proposed that the machinery and adjustments and terminology of tax administration be employed in the working out of the plan; but, in theory and in substance, no new tax is advocated, but only that the rents upon the public estates be collected and applied to the reduction or the displacement of the taxes now collected.

If, now, the proposition may be taken as established that in ultimate analysis the single tax is really not a tax at all, but is

merely an assertion on the part of society of its right to collect the rents upon its properties, the foundation has been laid for some further generalizations extending, both in theoretical and in practical significance, far beyond the limits of the single tax discussion. I freely admit that, confined solely to the land rent problem, the inaccuracies of thought involved in the name "single tax" are not matters of transcendent importance.

But the broader truth awaits recognition not only that the appropriation of unearned increment values is not taxation, but, still further, that the principle of appropriation is really not possible of application through taxation.

It has long been recognized in the business world and is now belatedly receiving acceptance in theoretical discussion, that the value of any income-paying property rests ultimately not upon cost but upon earning power — that cost gets into the case, if at all, only as bearing upon the relative supplies of productive properties and thereby upon their earning power, and that the market value of any property is merely the present worth of its more or less confidently expected future earnings.

It follows from this capitalization principle that any tax deduction from net income must reflect itself in a proportional fall in market value. Doubtless, however, it must be admitted that, if the tax is general over the whole field of investment, this capitalization principle will nowhere manifest itself in lower values; true, the net income is everywhere lower, but the interest rate upon which the computation of present worth proceeds is a correspondingly lower rate.

This admission does not, however, affect our problem, which, by assumption, concerns only the effect of an especially high rate of burden upon the values of particular lines of investments. The single tax principle, at its extreme of application, would evidently, then, leave no value to be taxed. Even beginning in a partial application, the value of the property must immediately contract to correspond, and forthwith, for the maintenance of the original revenue, a higher percentage rate of tax will be required. The principle is merely that in so far as appropriation proceeds, there can remain no value to serve as tax-rate basis. Thus there is nothing for the case but to abandon the present worth expression of the income and to proceed directly against the income.

But for practical purposes all this is especially relevant to the problem of the taxation of corporate securities. Let it be assumed for the purposes of the argument — and the actual truth of the assumption need not at all concern us — that the bonds and preferred stocks of American railroads are, in most cases and upon the average, sufficient to cover the investment costs of creating the plants and establishing the businesses; it must follow, if the doctrine above stated is accepted, that the common stocks carry a market value representative of nothing else than the present worth of the hope of excess income. The problem in this case, then, is whether the machinery of taxation can be made to serve in securing to the public the incomes accruing upon these stocks.

Precisely this problem appears to have presented itself — though fractionally — to Bastable; he observes:

“Weighty is the fact that with a system of private ownership and a developed economic organization the titles to these unearned gains are in a constant process of transfer, and future prices are estimated in the prices given. The anticipated future movement of rent is registered in the price of land. Premiums on shares measure the gains from speculation or monopoly. Justice could therefore be attained only by taxing such increase immediately on its existence being noticed, an entirely hopeless endeavor.”

But increase of what — of the earning power, the actually accruing income from the property of the business? But it is pointed out by Bastable that these anticipated earnings were long ago capitalized into market values, and have since undergone indefinite transfer. The confiscation objection applies here precisely as in the land question.

But if by “such increase” is meant the increased market values derivative from the substance of things hoped for, but as yet unseen, and if it be intended that taxation should forthwith step in to appropriate these increases, the difficulty is that, upon this assumption, these increases will never manifest themselves; if the certainty exists that, when these generous revenues shall actually accrue, the State will bestir itself to intercept them, market values can never rise in foreshadowing and announcement of the coming event. Thus market values

can disclose the promise or the actuality of the excess revenues only upon the assumption that no remedial action has been or will be taken against them. And if, contrary to the market-registered expectation, there is finally applied a remedy, this remedy must work the sudden confiscation of market values long generally traded in, but now lodged deflated in the hands of those investors least shrewd in political forecast.

If, however, doubt exist as to the future policy to be governmentally adopted, the valuation of the stocks in question becomes nothing more or other than a great game and gamble upon this issue. When faith in public drowsiness flourishes, or when confidence waxes in the possibility of somehow controlling the intermediaries between public opinion and its legislative expression, stocks will be value-strong in the prospect of future high returns. When, however, turbulence of public opinion becomes especially marked, or some truculent executive gets especially strenuous, there befalls a stock panic, and together with this, if conditions are favorable, direful secondary effects and reactions.

It is, then, evident that neither the forward-looking nor the backward-looking application of the tax principle can avail as a solution of the unearned increment problem. The only thing possible is the adoption of such measures in advance as shall forbid, either as capitalized present worth or as later collectible income, the emergence of the unearned increments in question. There must be permitted neither the actual distribution nor even the menace or the promise of a distribution of these excess revenues. The methods must be entirely anticipatory and preventive, whether by regulation of rates, or by sliding scales of franchise charge, or even by the still more drastic and possibly less effective or less practicable devices of radicalism. At all events, the present happens to be an especially opportune time for coming to realize that so long as society shall neglect or refuse to accept and to enact and to proclaim this principle of social appropriation, so long is society electing to stake its financial and industrial stability, not merely upon the assumption that for the indefinite future society is going to allow itself to be limitlessly plundered, but also that the investing public will regularly and continuously rest unperturbed in this conviction.

SOME GENERAL CONSIDERATIONS CONCERNING SOVEREIGNTY AND TAXATION

BY PROFESSOR LINDLEY M. KEASBEY

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THE question uppermost with us in Texas is the taxation of corporations. An argument in favor of the Williams bill, brought up in our last legislature, for the taxation of intangible assets has been prepared for this Conference by my colleague in the university, Professor Samuel Peterson — which paper I beg leave to read by title. For my own part, I have little of practical import to contribute. As I see it, this question of taxation has become so involved with the antecedent question of sovereignty as to cause all sorts of confusion — confusion concerning the sources of sovereignty, confusion concerning the incidence of taxation. To clear such confusion so far as I can, I propose to present for your consideration a series of postulates.

In the first place, to distinguish between a contribution and a tax: equals contribute to a common cause, superiors impose taxes in their own interests. In the second place, concerning sovereignty: where equality prevails, the State is democratic in character and sovereignty is exercised by the masses; where inequality prevails, the State is oligarchic in character and sovereignty is exercised by the classes.

Our American system of taxation (if system it can be called) was established under conditions of equality, when democracy prevailed, and — naïvely enough — we have proceeded on the same hypothesis ever since. As a matter of fact, inequality entered in from the outset, with the result that, superiors, oligarchs always, — aristocrats in the South before the war, plutocrats in the East since the war, — have endeavored in one way or another, and with considerable success, to impose taxes upon the people.

We assume the sovereignty of the people; how is it possible, then, for the many to be imposed upon by the few? Because sovereignty shifts as easily, almost, as the incidence of taxation. As the all-but-forgotten Harrington expressed it: "Empire

follows the balance of property," or, as I should say, sovereignty pertains to productive power. Now productive power is of three sorts: personal power — muscular and mental — which is labor; physical power — mechanical and generative — which is derived from land; and social powers — selling and purchasing — which are called capital. In the natural state, when land was free and capital all but non-existent, labor alone prevailed. In these halcyon days, laborers were all but equal, there were no taxes, and all contributed to a common cause. During the proprietary period which followed, land became appropriated by proprietors, who possessed sovereignty because of their monopoly of the mechanical and generative powers of production. Therefore they were in a position to impose taxes — in the form of tributes and rents — upon the laborers. Since the institution of exchange, the commercial era has come to prevail, and, sad to say, the social powers of selling and purchasing goods — capital, so called — has come to be monopolized, like land before. Capital being nowadays the dominant productive power (representing as it does the other two) sovereignty pertains thereto; and capital being controlled by corporations, corporations exercise such sovereignty — in the name of the masses, mind you — we are ruled by a plutocratic oligarchy operating under democratic forms.

In circumstances of such sort, the people propose to tax corporations — an absurdity on the face of it! Since taxes cannot be imposed except by sovereigns, to impose such taxes the people must make themselves sovereign. To make themselves sovereign under commercial conditions, the people must control capital, which is the source of such sovereignty. All of which is obvious enough, but how? Through the socialization of capital; there is no other way. Regulation, even taxation, is irrelevant so long as sovereign power belongs to the corporations which are to be regulated or taxed. Substitute public for corporate ownership of capital, sovereignty will shift of itself from corporations to people. In which case, under the conditions of the future social State, all being rendered relatively equal once more, taxes will become contributions again. All this is ideal, revolutionary, perhaps, but from such study as I have made of the subject, this seems to me the only solution.

THE TAXATION OF INTANGIBLE ASSETS IN TEXAS

BY PROFESSOR SAMUEL PETERSON

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THE present movement for the taxation of what are called the intangible assets of corporations is due to the fact that the ordinary, general and *ad valorem* property tax, when applied to corporations, especially of a monopolistic character, does not work satisfactorily. The *ad valorem* property tax, levied in the ordinary way, does not fit railroads, telegraph and telephone lines, express companies, etc., and this new idea of taxing the corporate excess is an effort to develop a system which will fit them.

Now, let us see exactly the nature of this tax, what it is and what it purports to do. It has been said that this movement is due to the present deficit, and that there are other and better ways of taking care of that. I dare say that this bill to tax intangible assets has nothing to do with the deficit and would have been introduced had there been a surplus. It is not a peculiar, local movement; it is a movement that is general throughout the most progressive portions of the whole country, those portions most advanced industrially, where corporations are becoming more and more the form of industrial organization. The movement has already in many States reached the point where the principle has been enacted into law, and it is only a question of time, of weeks, months or years, when it will be adopted in this State. (It has been adopted already in Texas in the case of national banks, and sleeping, parlor and dining car companies.) I do not say that this Williams bill, or any other specific bill, will be enacted into law, I do not say that it ought to be, but I say that sooner or later the principle upon which it is based will find adoption by the legislature as certainly as there is the spirit of progress among the people of Texas.

Now, what is the nature of that property which is sought to be taxed by this bill? There seems to be something mysterious about intangible assets, but the mystery is all in the name. As a matter of fact, or theory, there is no more of an intangible asset about a business lot on the avenue here than about a railroad. The value of a lot upon the avenue depends upon hundreds of various influences. It depends upon this Capitol being here, upon the university, the insane asylum and other institutions being located in its vicinity. It depends upon this being the county seat. It depends upon the number and character of the people living within a radius of many miles, and upon other industries. Remove all these things and the value of that lot would melt like a snowflake in the Gulf of Mexico. The value of a railroad is due to similar considerations; it depends upon the cities and towns along its route, on the fertility of the soil, on the character and industries of the people. As these elements increase and improve, the value of the railroad goes up, just as the value of a business lot increases with increasing population. The parallel is complete, the only difference being that one is merely an inert piece of land, while the other is a going concern. The same parallel holds in the case of a street railway, a telegraph or telephone line, gas works, an electric plant, an express company, and all the rest, except so far as modified by there being more of business organization and less of tangible property.

What about taxation? If a business lot and a railroad line are practically identical in character as regards value, it ought to follow that in taxing them on their value the same principle should be applied. The business lot should be assessed on its value, and the railroad should be assessed on its value. That is clear. And that is exactly what this scheme for taxing the intangible assets seeks to effect. The central aim and the controlling purpose of the whole movement is to get at the real value of the railroad and assess it.

Let us see, in assessing a business lot how do we determine what it is worth? By finding out what it would sell for. Let me ask if that is the way we have been determining the value of railroads in assessing them in this State. We all know there has been no attention paid to the selling value, and

for the very good reason, in the case of railroads, that no railroad is entirely within any one county. Trying to assess a railroad by the sections of it lying within different counties would be like taking that business lot, dividing it up into a hundred arbitrary pieces, of all shapes and sizes and positions, and then trying to assess each one as a separate independent tract. A pentagonal piece in the middle of the lot, taken in that way, would have practically no value at all. (When the revised statutes require a railroad company to give the assessor of a county a sworn statement of the length of the railway within the county and the value thereof, it is like taking a man on to a lot of his, marking off a piece four by six in the middle and making him swear what it is worth.) But suppose the laws and political boundaries were such that it should be necessary to assess each piece separately, what would be the proper thing to do? The only method worthy of mention would be to learn the value of the whole lot and then assign to each of the hundred parts such proportion of that value as its size and position would naturally demand.

When you get to the bottom of this intangible proposition, that is all there is to it. It is nothing but an attempt to get at the real value that ought to be assigned to each part of a road, and correct the necessarily insufficient and erroneous estimates made by assessing an arbitrary part of it separately. On account of state and county lines, and federal and state constitutions, it is impossible to assess a railroad as a whole, that is, to treat it as a business lot. But the same result is sought to be attained by allowing each county and each State to tax the railroad property within its borders as if that property were separate and independent wholes, and then, knowing that these are only parts, and knowing that in assessing them as parts their real value has not been determined, ascertaining their real value by learning the value of the whole and correcting these separate assessments by adding to them enough to raise their assessments to whatever is shown to be their proper value.

I have not time to take up the different kinds of corporate property inclined in this plan of taxation and apply this principle to each. It is evident that telegraph lines, express com-

panies and the like, which extend through different counties, are within the explanation and the application. But street railways, gas works, electric light plants and others found entirely within a county or city, — these, so far as geographical limits are concerned, can be assessed as a whole by a single assessor, — why should they be included in such a scheme?

Because the same old question is involved — getting at the real value, finding out what it will sell for. If the assessors were allowed to take the whole plant, say of a street railway, and assess it in a lump, there would be no necessity for its inclusion in this scheme. But here again there is often this splitting up of the whole into parts — parts whose character is such that it is impossible to tell their value by taking them separately. And if he did assess the whole in a lump, how would he determine its selling value? Take the Austin street railways; it is clear that in trying to learn what they would bring in the case of a sale, the assessor has a task somewhat different from that of determining what an avenue business lot would bring. There are a great many lots, more or less alike, some of which are actually sold from time to time, and from those sold the values of the others can be ascertained. Not so a street railway: there is only one of its kind in a place, and as to sales, they are practically never sold. If a man wishes to acquire a street railway, he does not buy it outright; he buys the stock which represents it, and thus indirectly acquires it. What follows? Simply that in deciding on the value of a street railway, recourse must be had to that which represents it, the stock, or, if there are also bonds, the stock and bonds. And that is precisely what this plan of taxing the so-called intangible assets is aiming to bring about.

But it is said that the value of the whole cannot be determined by the value of the stock and bonds. It is said that the values of stocks and bonds fluctuate on account of crops, storms, strikes, fires, wars and a hundred other things. But how is this any different, except in degree, from the case of a farm, the value of which fluctuates on account of crops, weather, and other conditions, generalized into good or bad times. Of course we know that there are artificial influences brought to bear to make stock go up or down, we know that there is such a thing as stock

manipulation, and that something which has a great deal of value may be made to appear to have but very little. In Philadelphia the machine politicians managed the city gas works in such a way as to make the people believe that it would be an act of generosity on the part of private individuals to organize a company to take it off their hands. Jay Gould amused himself by doing the same with railways from time to time. The same can be done with a factory, a store, a bank, a farm, by unscrupulous individuals. I am happy, however, to believe that such individuals are less frequent than they are prominent, and it seems to me that in elaborating a system of taxation it would be improper to turn aside simply on their account. What is desired is to get at the real value of the railroad, and this value, I believe, can be determined accurately and satisfactorily by taking the value of its stock and bonds, and in no other way. It is not necessary to take their value at a time when the stock is being manipulated. These manipulations are always temporary, and it is quite possible to determine whether a given value is a natural or an artificial one.

It is said so far as the railways of Texas are concerned that their stocks have no value except as a means of controlling the property; that a combination of individuals buy the stock in order to get control of the property, otherwise it would not sell for anything, because there have been practically no dividends paid on it. All this, however, does not affect my argument. It is the custom in this country to raise all the money necessary for a trust, a railway, or any other great corporation, by the issuance of bonds, using the stock merely for purposes of control and as representing the profits that the future is supposed to hold in store. If, in striving to arrive at the true nature of a railroad, we should confine ourselves to the capital stock, leaving out the bonds, this objection would be quite relevant. But inasmuch as the bonds are included the objection is quite irrelevant.

And there is another point. I should like to know just how, apart from the value of the stock and bonds, we can arrive at the true value of the property. This is a point on which we have no light. If the answer is the selling value, then, I repeat, there is no satisfactory method of determining the selling value apart from the stock and bonds. Perhaps, however, some one may

suggest the cost of building the road or plant, or the cost of reproducing it. As to this, I wish to say that it would be just as reasonable to assess the owner of a business lot on what it cost him as to assess a railroad, a telegraph line, a street railway or gas works on the basis of cost. That is no proof of what it is worth. In Philadelphia, up to 1897, the cost of the construction and equipment of the street railways had been about \$36,000,000, but the market value of their stocks and bonds was \$120,000,000. Remember that railroads, telegraph lines, street railways, gas works, waterworks and the like, are monopolies, and values grow by reason of increasing population, just as does the value of a business lot.

But some one will call attention to the fact that all the time I am talking about a business lot and its value, the assessor is assessing it, not at its real value, but at 30 or 40 per cent of its value. There is nothing in all I have said to prevent him from assessing a railroad or a street railway at the same percentage. All I am insisting upon is the importance, the necessity, of his knowing its real value, for otherwise how could he know what is 30 or 40 per cent thereof? In order to make the assessment at some definite percentage it is absolutely necessary that he should know the real value. Equality of taxation between the business lot and the railroad is a practical, as well as a theoretical, impossibility without a knowledge of the real value of each.

I wish to say in closing that it is not a question between a perfect system and none at all. If you are looking for a perfect measure, one that will work with mathematical accuracy, if you intend to reject anything that falls short of this, then you may as well turn to other matters at once. This world is a world, not of perfection, but of progress; perfection is nothing but a goal toward which we strive; this striving we call progress; when perfection is reached, then progress is at an end. In this world there is no such thing as perfection at the start; we must start with that which is rude, imperfect and full of faults, and then by persistent improvement, by elimination of faults, gradually approach perfection. The bicycle of to-day was not invented all at once. It began with two wheels connected by a bar — a mere toy, without steering or propelling apparatus, it was labo-

rious and dangerous and absolutely useless. But here a little, there a little, year after year, through scorn and ridicule, improvement went on, until, in the course of time, perfected in detail, it has become a machine of marvelous utility. Take the printing press found in the press rooms of our great dailies, running off fifty thousand eight-page sheets an hour; and yet without the rude imperfect beginnings of earlier generations, we know that press would have been as impossible as a university graduate that had never learned to read and write. And so in every department of human activity, and not least in the realm of legislation. Take the primary election law — if you had waited before passing it until it could have been perfected, we should have had to wait till the millennium, and then we should not have needed it at all. The only way to make progress is to make a start, necessarily crude and imperfect, but doing the best we can, and with the experience of succeeding years, here a little, and there a little, gradually bringing it nearer and nearer to perfection.

The question now before us is not whether the measure is perfect or imperfect, but whether the principle upon which it works is right or wrong. If it is wrong, reject it. If it is right, adopt it in the best form we are now able to construct, and remember that "Rome was not built in a day."

MULTIPLE TAXATION AND TAXATION OF CREDITS

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I HAVE no intention of proposing a complete system of taxation. The existing American system cannot be suddenly revolutionized. It is at most possible to indicate certain directions along which improvement may be introduced. There can be little of new in taxation — at least little that has not been tried somewhere in Europe or America. Reform will undoubtedly follow either the line of the income tax or that of business licenses, transfer taxes and land tax. It seems already to have struck out in the latter path. The inheritance tax is already nominally adopted, and will grow in favor no matter what other taxes are adopted.

The object of this paper is primarily to justify and emphasize the importance of the taxation of credits. Political economy has too much confined itself to description of the material limits and influences of industry; and especially has its definition of capital as material goods offered a seeming justification to the legislator for taxing things instead of taxing the economic control lodged in the hands of the taxpayer.

It is to this phase of the tax problem that I desire to draw attention. Economic control is largely a matter of credit; either that kind of credit which is granted by the bondholder and stockholder, or that given by the noteholder or billholder. In some form or other the control of industry, and consequently and most naturally the first claim upon the surplus product, is that of the capitalist rather than that of the proprietor; but the actual course of business has divided stockholders into majority and minority stockholders. In equity the minority stockholders should stand with the bondholders as ahead of the proprietors — the majority stockholders.

In dealing with the question of taxation of credits it is necessary to consider whether they can best be taxed under the existing property tax or under the two tax systems toward one of which we are inevitably tending in America — the income tax or licenses, transfer and land taxes. Unavoidably, therefore, these tendencies are examined at some length. But in the first place it is necessary to expose the evils of the property tax and especially its lack of adaptability to the taxation of credits. For the present purpose, it is a matter of little moment whether the taxes under discussion are laid by the government of the United States or by those of the States. It is a question of taxation of persons rather than one of raising and spending governmental revenue.

Under the simple conditions that environed our forefathers, a general property tax was a most logical institution. In early days economic resources were uniformly land and its products, houses, and tools, and, in exceptional cases, ships, and a little cash. Land predominated to such an extent as to form the rule. The term "property tax" therefore, meant "land tax." But the term "property" has spread over all the multiplied forms of production and consumption goods as well as over the various sorts of contracts held by persons on the faith of the owners and of the moral pledge of the value-produce of these goods. The convenience of the law has been satisfied by this leveling of all sorts of economic control under one rubric; and popular use of language has followed the lead of the law, as the only available guide. Political economy as a theory is only gradually coming in touch with the industrious classes, whereas they have been in close contact with law and litigation and its use of terms from earliest times.

I believe that this use of a blanket term — "property" — borrowed from the law, not only proves that men think primarily in terms of their personal rights rather than in terms of economic efficiency, but explains why the multiplicity of sources of income has been neglected by our tax laws until we have entirely outgrown the latter and a reform is demanded in the name of justice, of self-respect and of common morality.

The failure of the pseudo-legal theory that the same kind of tax is applicable to all sorts of sources is clearly indicated by

Professor Seager:¹ "But, as has just been shown, in practice, especially in the more developed sections of the country, personal property very largely escapes the tax. The general property tax becomes in consequence a tax on real estate, upon certain kinds of personal property, and upon the conscientious owners of all kinds of personal property. To determine who pays this tax we must go even a step farther and describe it as a tax on land, on buildings, on certain sorts of personal property, and on certain sorts of personal property owners."

A diplomatic report to the British secretary for foreign affairs recites: "Strange anomalies and singular abuses result partly from the viciousness of the tax law and partly from the embarrassment of the assessors, who are confronted with such objects of taxation as government bonds (*sic*), account books, money loaned at interest, cash in hand, so easily concealed or disposed of."² Says Leroy-Beaulieu: "We have examined the property tax in the United States. Modern taxation has seldom invented a more stupid instrument. . . . The tax is not levied solely on what some French theorists call fixed capital, — that is to say, immovables such as land and buildings, — it falls also on merchandise, foods, even household provisions beyond a certain sum. An inventory of these provisions has to be made — of these raw materials and objects of all sorts — things that are evanescent and perishable. It is needless to say that for the most part the whole stock of goods of a merchant is not his personal property; often they much exceed his whole fortune; nevertheless he must pay on them all. Of course he will make good by raising his prices; and in that case it would be much simpler to put an *octroi* on certain goods; that would permit the convenience of the (bonded) warehousing system. The property tax is unequal and complicated. It is necessarily a source of profit to some while it calls on others for great sacrifices. Nevertheless it is not very productive. The rate has to be raised very high in order to get small returns. In the city of Dorchester it calls for $\frac{3}{4}$ per cent of the capital value; and if reliance were to be placed on this tax alone for all the expendi-

¹ "Introduction to Economics," p. 550.

² Cited in Leroy-Beaulieu, "Science des Finances," fourth edition, I. p. 499.

tures of the cities, counties, States, and for the Union, it would certainly have to be quadrupled, which would carry it to 2½ per cent of the sum total not only of the fixed capital, but of all goods, merchandise and provisions." ¹ I may add that this tax partly accounts for the very high price of articles sold at retail in the United States.

A protective tariff has bad features, but they sink into insignificance beside the enormities of the property tax. It is under the ægis of this tax that the disregard of interstate comity known as "double taxation" has arisen. "If a citizen of Massachusetts has a farm in New York and cattle on it, the Massachusetts authorities admit that the farm is in New York but maintain that the cattle, being personal property, are constructively located in Massachusetts, and tax them there. But if a citizen of New York has cattle in Massachusetts, these same authorities change their theory of *lex loci*, and tax the New Yorker's cattle all the same." ²

There are, indeed, some other countries that have a property tax, but in these countries it is very mild and is used simply as an auxiliary to the more important taxes. For example, in Switzerland, in most cantons, the property tax and the income tax exist side by side and complement each other.³

The property tax is a direct tax and supplies local needs, whereas the American national government is chiefly sustained by indirect taxes such as customs duties and the internal revenue excise. In this broad demarcation the United States has followed a necessity that has seemed conclusive to most European states also. The general government must logically levy its tax under those circumstances that are universal, such as commerce and consumption; whereas in the localities the economic status of the citizens severally can best be known. As additional resources, the localities have their domains, parks, local public service monopolies, their water, gas and electricity. The sum of these sources of taxation is so productive that the state governments in this country and the general governments abroad are constrained to limit the abuse of the exercise of the taxing or borrowing power by the localities. Consequently, the intro-

¹ Leroy-Beaulieu, *op. cit.*, pp. 498-499.

² *Ibid.*, p. 499. ³ *Ibid.*, p. 500.

duction of a new kind of tax should be made by the authority of the whole State,¹ and limited by the State, as is the property tax at present.²

The evils of the evasion of the property tax are too well known to need repetition; but it may be well to call attention to an abuse of the tax commonly perpetrated by the public authorities themselves: when a city has reached the limit of indebtedness prescribed by law, the city authorities may raise the assessments of all the citizens and thus increase the borrowing power of the city. This process may go on without assignable limit and without raising the amount taken in taxes (except in so far as larger interest-payments call for more) by simply lowering the tax rate in the same ratio as the assessments have been raised. Thus the property tax facilitates evasion of legal restriction on borrowing and on ultimate taxation. Again, when a state constitution grants a one or two mill levy for the support of a state university, the fiscal authorities may decrease the assessments throughout the State in order to keep the income of the university at a minimum. But neither the State nor the minor localities are prejudiced by this lowering of valuations, since the state and local rates are raised accordingly. The state legislatures make ineffectual attempts to place a minimum limit on the valuations made by the assessors; but these limitations are, from the indefinite nature of the property tax and from the loose control over assessors, merely directory and carry no enforceable obligation. The property tax results in an unconstitutional delegation of legislative powers by the state legislatures. Reform lies in the recasting of the whole scheme of taxes and assessments together.

The property tax, as we shall soon see, has not changed so far as it is a charge upon the value of "property," during a large part of our national history. Leroy-Beaulieu says that it would have to be quadrupled to suffice for all national, state and local expenditures, arguing from data of Massachusetts about the middle of the last century. It is certain that at the present time, when the expenses of government are growing so rapidly, that it would not suffice. In the year 1902 the expenses of the States and territories, counties, cities and other minor civil divisions

¹ Meaning either "state" or "general" government.

² Leroy-Beaulieu, *op. cit.*, p. 710.

of the United States involved an expenditure of \$1,156,447,085.¹ Of this enormous sum three quarters or \$867,333,813 was raised by the property tax and the other quarter was raised by special property and business taxes, poll taxes, liquor licenses and other licenses and permits, fines and forfeits, subventions and grants, donations and bequests.² If we compare the amount of \$867,000,000 with the total expenditure of the nation and all its parts, \$1,773,000,000, we find that it is almost exactly one half, and that by doubling the property tax we could abolish our franchise taxes, our liquor licenses, our customs tariff, our internal revenues, and give away our whole public domain.

It is, however, doubtful if the property tax could be doubled, not to speak of quadrupling it, as did Leroy-Beaulieu in his hypothesis. He calculates that even a single tax on revenue could not be made to meet the French budget even though the latter be subjected to drastic pruning.³ In the middle of the eighties he estimated that the French land tax amounted to 10.36 per cent of the net income of the land including houses and other buildings. He also considered that the revenue from the land in France was at most 3 per cent. According to Du Plessis de Grénédan,⁴ French agriculture taken as a whole returns but 2.40 per cent on the investment. But taking the higher estimate of Leroy-Beaulieu, 3 per cent, and multiplying by 10.6 per cent, we arrive at .31 per cent as the proportion of the capital value of the land taken by the French land tax. This is regarded by him as a point beyond which a good land tax could not be carried.⁵ If we turn, however, to the American figures we find that our statistical authorities have estimated the average property tax for all the States and Territories of the United States at .74 per cent of the true value of the property.⁶ For the purpose of comparison of amount raised (but not of justice toward individuals) we may roughly compare the American property tax to the French land tax. We therefore

¹ "Wealth, Debt and Taxation," in Special Report of the Census Office, p. 963.

² *Ibid.*, p. 967.

³ "Science des Finances," I, p. 179.

⁴ "Géographie Agricole de la France," p. 106.

⁵ "Science des Finances," p. 331.

⁶ "Wealth, Debt and Taxation," in Special Report of the Census Office, p. 850.

perceive that the American property tax already exacts over $2\frac{1}{2}$ times the proportion exacted by the French tax.

But we are not to infer from this comparison that the property tax is peculiarly elastic simply because a much larger rate has been imposed in the United States than in France. Of course the fact that we are not burdened with a multiple system of taxation does make it somewhat easier for us to pay this non-descript tax of ours. Anyhow it enables us to hit some people harder with it.

If our tax experts at Washington have correctly estimated the variation from true value of the local assessments, there has been practically no advance in the rate of assessment of property in the whole United States since 1880. The figures are:

1880	\$0.72
1890	0.73
1902	0.74

The inference is that the tax has not advanced because it could not advance, and that all attempts to raise a very large tax in this way must fail. The well of taxation opened by the property tax has been pumped to its lowest level from very early times. It is true that the nominal rate ¹ has been steadily rising since 1880, but the assessments have been correspondingly depressed, so as to leave the real rate constant. The real rate had, however, advanced considerably in certain States such as North and South Carolina, Georgia, Florida, Kentucky, Tennessee, Alabama and Mississippi. In no State apparently has it declined so much as in Nebraska.²

1880	\$0.73
1890	0.65
1902	0.52

The property tax, then, is raising a sum of money which in the aggregate looks very large. The real question is, however, not so much the gross amount of the tax as the justice of it. A tax which is reaching the limit of practicable enforcement is *prima facie* an unjust tax. Only mild taxes are endurable.

¹ "Wealth, Debt and Taxation," Special Report of the Census Office, p. 849.

² *Ibid.*, p. 850.

Again, a tax which is not specific, which is not what it claims to be, and which forces public officials into arbitrary acts and regulations and habits in its enforcement, putting upon their shoulders the responsibility nominally assumed by the legislators, is *prima facie* an unjust tax. It needs little argument to show that such a tax not only raises a very small revenue compared with what the country could easily bear if scientifically taxed, but it actually stands in the way of a well-balanced system of taxation which would be many times as productive while much less onerous.

The great defect in the property tax is, as already noted, that in modern times individual control over social income has assumed such multifarious forms as to be indescribable for purposes of taxation, at least under the general term of "property," and to be incapable of assessment by the same set of assessors. It is plain that the house-to-house visit of the assessor can reveal nothing more than houses, lands, factories, machines, goods and chattels. Now in a great many of these cases, if the debts were allowed to be set off, as they should be, in theory, there would be nothing left to assess. Consequently, sometimes by statute and sometimes doubtless by local custom, for certain classes of properties, the taxpayer is allowed to set off debts. He may do it in many places if he is a mortgagor as to his mortgage debt; and in some places he may do it if he is a corporation as to stocks and bonds. Theoretically this allowance should be made for every kind of a debt. It is not made for certain kinds of debts because they cannot be reached at the debtor end. No system of assessment can discover the bills of exchange, promissory notes or demand notes in the hands of individuals, and no proposition that I know of has ventured to tax them in the hands of the banks. Right off at the start therefore we perceive that the property tax falls of its own weight into a tax on lands, stocks of goods, machines, furniture, means of transportation, and other tangible goods, and into a special tax on those obligations which are of quasi-public record like corporation stocks and bonds. In part, at least, this has been the practical result. Our democratic legislation therefore, which seeks to include everything, has resulted in merely scratching over the surface of the real

property and the buildings, and, with the help of a little legislation, the holders of corporation securities.

Perhaps it is a good thing that our taxation is so inefficient. The magnificent sums that might be raised in this country by "a balanced tax ration" would gladden the heart of the treasury if the treasury had any use for them, but would not assist prosperity. Nevertheless, large sums are continually demanded by the increasing activities of our public authorities, and it is our duty to point out how in raising them we may at the same time reform the existing injustices which strike persons engaged in certain classes of enterprise so unequally. The American property tax has dwindled down, said Leroy-Beaulieu some time ago, to a "partial and rather light tax which can only raise a small part of the fiscal wants of the Swiss cantons or of the States of the American Union; it is analogous to our (French) land tax and to our house tax; in practice at least it does not differ greatly from them."¹ Doubtless Leroy-Beaulieu minimizes the fruitfulness of the property tax in the United States.² Indeed, in another place, he states that in the towns of the American Union the property tax often reaches 30 or 40 per cent of the rental value of a house, that is to say 3 or 4 per cent of its market value.³ He considers that to be a good thing if it is combined with a comparative absence of taxes on laborers' necessities and reasonable enjoyments. Better high rents and untrammelled commerce, cheap and unadulterated foods, than the reverse state of affairs.⁴ But the property tax raises not only house rents but the prices of necessities.

Not only is the property tax unjust because it does not tax what it professes to, but because it taxes things that are extremely difficult to assess even though there be no concealment. It is comparatively easy to find the market value of a stock of goods in a store or of any active capital used in production, but very hard to estimate a capital, i.e. a principal value for articles which neither are nor could be capital; such articles possess a merely hypothetical value and are subject to the most capricious estimation; this is true of all fixed capital

¹ "Science des Finances," p. 219.

² *Ibid.*, p. 362.

³ *Ibid.*, p. 217.

⁴ *Ibid.*, p. 362.

which gives no revenue; its value depends on fancy and imagination and not on serious calculations; it is only reached by the treasury with difficulty and should be taxed, if at all, very lightly.¹ In confirmation of this statement we need only notice the light-heartedness with which our boards of equalization and very notably our county supervisors hoist or lower a citizen's assessments after the very briefest consideration. And why not? Longer consideration would not help them on an insoluble problem.

And even where the property is productive, capital value is very hard to arrive at. The United States Census Bureau reports, "All of the objections to the statistics for capital in manufactures apply with greater force to the statistics for mines and quarries, and they may be summarized as follows:

"1. It is impossible to define the word 'capital' for statistical measurement so that it shall be tangible, restricted and uniform.

"2. The inquiry creates more prejudice and arouses more opposition to the progress of the enumeration than all of the other inquiries united.

"3. The value of 'fixed capital' — land and buildings — is dependent upon conditions of which a census can take no cognizance.

"4. The difficulties attending the collection of statistics for live capital — 'cash on hand, bills receivable, unsettled accounts, etc.' — preclude the possibility of reliable results.

"5. It is impossible to eliminate the duplication in gross assets and credit capital.

"6. Good will, patents, mining rights, etc., are forms of capital for which no satisfactory value can be obtained.

"7. Many mining companies have investments other than of the amounts required to carry on their business and yet constituting a part of their capital, such as railroads, steamships, and timber lands, and it is impossible to segregate the capital that pertains strictly to mining.

"8. A number of mines are operated under leases. The lessees furnish the census reports, but have no knowledge of the mine or the capital invested by the lessee in land, shafts, machinery, etc.

"9. The value of a mine is due chiefly to the character and amount of ore supposed to be in the earth, and is, therefore, largely speculative."²

¹ Leroy-Beaulieu, *op. cit.*, p. 217.

² "Mines and Quarries," Special Report of the Census Office, 1902, p. 74.

But ordinary assessors, appointed "politically," are supposed to be able, without previous training, to make capital valuations which experienced agents of the Census Bureau find impossible!

It is but a step from the property tax to the income tax. It is in this very matter of difficulty of valuation that the latter is superior to the former. Here is no question of consumption goods whose value is measured only by the pleasure they give and for which there is no frequented market. The value of a race horse is whatever the owner may chance to get for that individual horse. A horse that sells to-day for \$10,000 may be sold to-morrow for \$20,000 or for \$200. Taxation should not attempt to control the caprices of men, and the State always finds such attempted discrimination unprofitable in revenue. On the other hand, the income which a man enjoys is much more easily ascertained. Every man keeps some sort of accounts which measure the income in dollars and cents. It is not, of course, proper for government to inspect private accounts, which the certainty of the income makes it more easy for the taxpayer to render an exact account to the assessor. In the taxpayer's argument with his own conscience, Conscience has a much better case in the instance of the income tax than in that of the property tax. Then again, if the public authorities make inferences as to income from a man's style of living, their decision is likely to be submitted to with tolerable grace.¹

Economists agree that capital is merely a derivative of income and not the other way about. Scientifically speaking, capital is a hypothetical quantity, while income is an ascertained quantity. A man's income may be paid to him in the form of bank deposits, but those bank deposits always arise from the sale of products, that is to say from what is at the very time being circulating capital which has a large and steady market. While a race horse in the hands of a turfman has only a fancy value, yet thoroughbred horses may be bought of the breeders at fairly constant market prices, at least after they have been graded into two or three classes. It is in the market for circulating capital, then, that values primarily arise, and it is in circulating credit that incomes are paid and received.

In the simultaneous breaking down of the property tax and

¹ Cf. Leroy-Beaulieu, *op. cit.*, p. 498.

development of a multiple system of taxation, which are going on in this country, the income tax is asserting itself in a concealed form beneath the property tax. For instance in Montana, Nebraska and New Mexico, insurance companies are "taxed on net receipts or on premiums less losses and expenses at the same rate as personal property."¹ Similarly "railroads are taxed for state purposes on their gross (or net) earnings (other than taxes merely to defray the expenses of railroad commissions)" in several States.²

Hard experiences with tax collectors from over the sea undoubtedly convinced our forefathers that the idea of multiplicity in taxation had been carried decidedly too far. But there is such a thing as carrying simplicity of taxation too far. When a "single" tax carries with it the implication that all men are possessed of the same kind of property or property that can be taxed in the same way, it is time to call a halt on a system which pretends that that exists which does not. It is better to devise a few taxes which will meet certain classes of cases that are manifestly dissimilar. It is the property tax also that has led to those cases which are known as double taxation. The double taxation is the result of the false simplicity of the tax. *Multiple* taxation is necessary precisely in order to avoid *double* taxation. There is much error afloat as to the nature of double taxation. A man is not doubly taxed because he contributes to the State through two channels instead of one, nor is he doubly taxed because he pays twice as much this year as he did last. Double taxation arises only where one taxpayer is compelled to pay more than another who is exactly similarly situated.

The necessity of creating different kinds of taxes has already led to special taxes and to special agents for their assessment quite generally throughout the United States. Inheritance taxes are assessed through a special official in New York and perhaps in other States. Corporation taxes are assessed by a state board for certain classes of corporations or certain classes of corporate property. Business taxes and licenses have become common in the Southern States, which are obtaining a

¹ Plehn (Carl C.), "Revenue Systems of the States and Local Governments," in "Wealth, Debt and Taxation," p. 636.

² *Ibid.*, p. 637.

growing proportion of their growing incomes in this way. I have counted 188 of these taxes.¹ Of course some of these taxes, like liquor licenses, peddlers or circuses, are imposed in all or many sections of the country, but in general the license system is peculiar to the Southern States.

In the nature of things ever, tax is paid out of income. The assertion of a right to tax principal is nothing less than the assertion of a right of confiscation. I know of a case of an honest farmer in my State who had been assessed like his neighbors at a very small fraction of the estimated value of his farm and stock. But one year a new assessor appeared, a man either ignorant or mischievously inclined. The farmer was asked to state the value of his stock, etc., and made a reasonable and honest estimate of the same. The assessor put the assessment down precisely as given in by the farmer, who found himself suddenly mulcted for a sum exceeding his total income. He was compelled to leave the State. In practice, therefore, the property tax involves the right of confiscation. If this right were always exercised, the country would be ruined and the State soon find itself without revenue.

Income is necessarily the basis of calculation of the amount of taxation. Apart from distinction of kinds of income, such as is made in the schedules of the British income tax, let us for a moment consider the nature of the income that is taxed, with a view of discovering the relation of credit to income. Evidently when we say "income," we do not mean the whole future income accruing by virtue of a given investment, for that global income when discounted is theoretically exactly equal to the capital value of the tangible property. The only basis for meeting the current needs of governments is the current income of society; the expenses of government for one year must be met out of society's income for one year. For this purpose society is to be viewed as but an aggregation — a sum of persons; and what holds true of society holds true of each person; he must not be taxed on any other basis than income. Income is another way of saying "ability to pay"; and economists have agreed that ability to pay is the basis of taxation. Now let us consider the bearing of this conclusion on the taxation of

¹ The full list will be found in Plehn, *op. cit.*, pp. 639 *eqq.*

credit. Credit "represents" present material goods — it duplicates present material goods — only in a roundabout way. A mortgage bond represents the mortgaged land only indirectly. It has been usual for tax reformers to say that credit *represents* material property, and hence that taxation of both is double taxation. In other words, it is double taxation to tax the mortgagor to the whole value of the property and at the same time to tax the mortgagee on his mortgage-credit.

This statement I apprehend to be, strictly speaking, an error. A credit document strictly is the only visible representative of a definite future production. It is a contract for the execution of which, to be sure, either material or personal present guarantees are put up. The mortgaged land is but the material gage — like the bank reserve — out of which the application of the future returns of the land to interest payment is guaranteed. If the mortgagor fails to make good these payments, then the mortgagee has a right to foreclose on the land and sell it to a purchaser who expects to make good for himself out of it and who is in turn ready to pay down the discounted present value of the future payments on which the mortgagor is expected to continue in default, if one is to judge from his past conduct.

There is a sense therefore — and to my mind this is the most important viewpoint of the relation of tangible to intangible capital, in which credit is to be regarded as really and truly capital-wealth, and in which credit is to be regarded as primarily subject to taxation. According to this reasoning, the taxes should be levied primarily on the owner of the credit, and "double taxation," in the popular sense even, emerges when we also tax the gage, be it land, coin, or other tangible goods.

The common view is to regard the tangible thing as primarily the subject of taxation, and to consider that "double taxation" arises only when the credit is mulcted.¹ But this view clashes with the principle that value, the real basis of taxation, is the discounted price of unfinished future products, or at least goods which are in the market, which are certainly represented more truly by the contracts for their production — embodied in credit — than by finished material capital goods.

¹ Cf. Taussig's characterization of the popular notion, in *Political Science Quarterly*, Vol. XIV, p. 119.

The popular view also clashes with the principle that after all it is men that are taxed, not things. Taxation is morally on persons. Economic theories are at the best crude. They are matters of opinion and of academic debate. They are choice dishes for metaphysic *gourmets* and not designed for popular consumption. Certainly they should lie at the basis of our social systems, but should never interfere with common sense. When a theory causes manifest injustice, we must be guided by our good sense in the matter rather than by our theory. A theory simply directs our attention and causes us to inquire whether we may not profitably make a new departure. The theory just presented that credit is the primary basis of taxation, should merely open our eyes to the importance and validity of the taxes on credit and not lead us into attempts to tax credits that are manifestly untaxable. The science of taxation should be chiefly for the purpose of promoting justice between individuals. The raising of revenue for the State is perhaps of secondary importance in a discussion of systems. It is a consideration for the rights of the individual man that must chiefly claim our attention. It is certainly curious that the system of taxation which claims to be most realistic — the single tax on land — is the very one that offends most against private interests, for instead of taxing individual incomes it would take a *theoretical* surplus of value regardless of individual interests; and yet claims that no one can possibly be wronged by this rash application of a theory. A single tax on capital would be almost equally objectionable. Leroy-Beaulieu says that in France it would take 18 or 20 per cent of the income from capital. In case of landed capital in France it would amount to 2½ per cent of the land values.¹

Taxation is a bill of debt against industrial persons. The weight of the problem of taxation is precisely on the personal relation. In a large way we may speak of taxing the property or the income of the country. That is the way in which a state commission, or even a county or city board, must make their grand assessments of taxes. For their purposes the sum total of individual tax liabilities is reached by a short cut in their summation of the property or of the surplus production

¹ "Science des Finances," p. 218.

taxes — unauthorized by law except as the property tax authorizes any and every levy that local custom may fancy or the taxpayers in their indifference and preoccupation tolerate — cannot be indefinitely endured. This is a state tax, and upon the States devolves the task of bringing order out of chaos, certainty out of uncertainty, system out of haphazard. The property tax is become a name for what it is not; and the real taxes are nameless abominations, a hit-or-miss contribution laid on any property that strikes the whim of the local or state assessors. The broad question seems to be whether we shall abolish the property tax in favor of the income tax — under permission of a revision of the United States constitution — or shall allow it to wither away by carefully defining the classes of property, principally land and houses, to which it shall apply, and then consciously develop these specific taxes that have already arisen partly under custom and partly under legislative sanction. The latter system would practically amount to a land and house tax, plus an inheritance tax, plus a complicated system of licenses, including the franchise tax under the last head of licenses, plus patents or business taxes. The subject of business taxes, licenses and patents is a large one by itself, and requires a separate and elaborate scheme.¹ The States and cities would share these taxes. The cities would also receive an income from public service corporations — also a license or franchise tax. In this way the constitutional objection to a state income tax, that dog in the manger of American taxation, would be avoided. In this respect as in so many others the development of our institutions would follow the example of France — is, in fact, following it.

This is what is occurring and what seems likely to occur. In that case incomes from private credits — and these as we have seen are the primary and fundamental incomes — will still be insufficiently reached. Taxation, except in the case of corporation securities, will not be at the source of value, but at lower points in the stream. With all their elaboration of licenses and patents, registration or record fees, and stamps on business paper or stamped paper, the French have been unable

¹ Cf. "Science des Finances," p. 404, for the complicated system of French patents and licenses.

to reach private loans, except very occasionally and indirectly.¹ The fees for recording documents and the income on the sale of revenue stamps on legal documents and stamped paper amounted on the average to \$3.50 per capita in France, to \$1.65 per capita in England, and to \$1.06 per capita in Italy and Austria.² The holders of securities in France pay about 3 per cent of their revenue, but they have to pay in addition a transfer tax which in the case of unregistered securities takes the form of holding back an additional amount on the annual dividend. In practice the whole tax is a respectable one, amounting to 6 or 7 per cent of the dividend or interest. A bond of one of the great railroad companies was subjected to a subtraction of about one franc ten centimes on every fifteen francs of interest, which amounts to 7 or 8 per cent.³ To this tax we must add the recent tax on stock exchange transactions, which tends to increase the inequality between the taxation of corporations and the taxation of private businesses. It would be possible perhaps to restrict the operation of the recording transfer and stamp taxes to private businesses and to the leisure classes. In that case those taxes could be made somewhat higher. If it was found that inequality still existed, it would be possible to put a very moderate income tax on these classes, but it must be extremely moderate and put on purely for the purpose of equalization and without any design of placing the burden of taxation upon them. The doctrine that the classes that have accumulated capital and are using their income in some manner different from the production of material goods are of less use to society than those engaged in business and manufacture, is a dangerous one, especially in a wealthy democracy, for it is not true.

However, a thorough system of reaching income at the source — and I am not speaking of taxing dividends as they emerge from the corporations, a small part of the larger question of taxing credits — can only be introduced if the constitutional prohibition on state income taxes be removed. In that case the several States would strike out in the British path. There are advantages in the more radical plan. They certainly

¹ Leroy-Beaulieu, *op. cit.*, p. 419. Companies pay a tax on commissions of stocks. List of do-nothing capitalists. ² *Ibid.*, p. 538. ³ *Ibid.*, p. 423.

deserve a careful canvassing. If they seem great enough after due deliberation, the country as a whole may be moved to adopt this course, by permission of the federal Constitution and by subsequent action of the several state legislatures. However, as Leroy-Beaulieu says, an income tax should only be used as a tax to compensate for inequalities caused by other taxes. In the times of extreme national needs it should never exceed 4 or 5 per cent and should ordinarily not go above $2\frac{1}{2}$ or 3 per cent.¹ It is, of course, an inquisitorial tax. If the rate is high, concealment becomes universal and the cost of collection rises rapidly. The difficulties, however, of assessing an income tax are, as already remarked, much less than those of assessing a property tax. It brings in a large revenue and one which rises steadily with increase of population and wealth. Whether such a tax should be for the exclusive benefit of the national government or of the States is not pertinent to this discussion, which is limited to an inquiry as to how taxes may be arranged fairly to the individual. From the individual's point of view it makes no difference which of the rival governments to which he is necessarily subjected receives this or that tax. Under the property tax, tax dodging has acquired something of the respectability that smuggling enjoyed in early days; it is a revolt against iniquitous oppression. Under a moderate revenue tax it is tax dodging and nothing more.

The income tax with all its defects comes as close to taxing the main primary incomes as human ingenuity can suggest. It taxes the incomes from all investments and credits. It remains to discuss the bearing of the taxation of credits upon *double taxation*.

The popular idea of "double taxation" is that it consists in taxing at the same time the possessor of the machine and the man who derives the primary income from the machine, the creditor. This is a partial truth, so partial that it amounts to an error. Suppose that the mortgagor is taxed on the whole of his mortgaged property and that the mortgagee is taxed again on the face value of the mortgage, it is evident that the party of the first part and the party of the second part are held to pay

¹ Leroy-Beaulieu, *op. cit.*, p. 443.

their taxes out of the same piece of property. This may be *doubling* of taxation but it is not strictly double taxation. So far as our illustration has gone, it amounts simply to raising the rate on the property. But the next farm is not mortgaged. It therefore pays the original tax. It is evident that out of the first farm (supposing them of equal economic efficiency) must come twice as large a payment to the treasury as out of the second. The value of the first farm is considerably diminished so long as it is subjected to this increased taxation, while the value of the second farm is unaffected. The "double" taxation arises from the comparison. The rate has been raised on one group of interests and not raised on another situated next door.

This is clearly unjust and has long been recognized as such, and yet many American States have made no attempt to remedy the inequality. In some States the mortgagor is allowed to subtract the amount of the mortgage. In Nebraska, Governor Sheldon has proposed to exempt mortgages from taxation altogether, on the ground that capital is driven to those States where allowance is made for mortgage debts. This is certainly a fair proposition for the temporary disposal of this particular case of double taxation. It is, however, a makeshift. As already shown, credits are an eminently proper object of taxation. In this respect they resemble rents. As Professor Patten has well said, rent equalizes differences in space and interest equalizes differences in time. Would it not be better therefore to allow the mortgagor to subtract his debt from his assessment and thus bring mortgage taxation into conformity with a general system of taxation of credits? I admit that the proposition of Governor Sheldon is the more practical one in view of actual circumstances, since assessors in Nebraska are authorized to assess the land only up to one fifth of its true value. Evidently the only way out of the difficulty is to abolish the property tax, substituting a moderate land tax and house tax, so moderate that the true value would be assessed. In that case it might not be necessary to make allowance for the mortgage debt.

The evil of double taxation also arises where any credit is taxed both at the residence of the creditor and at the place where

the source of the income is situated. This usually happens where the two are located in different States. If the States would all agree to allow the subtraction of mortgage debts, or else to substitute a very moderate land tax for the property tax, the cause of the greatest complaint from double taxation would be removed.

Some States allow other debts than mortgage debts to be subtracted from the assessment. This is a move in the right direction. The reason why they have proceeded slowly in this matter is that under the property tax the total basis for taxation would be greatly diminished by a general allowance of this kind of set-off: while the holders of material property would be exempted, the creditors could not be reached in most cases. Since the current production of the country is almost entirely represented by a corresponding indebtedness in the form of commercial paper and other documents, a very large proportion of the property of the country would escape taxation altogether. But with a moderate land and house tax, a moderate business tax, and a moderate income tax, the last restricted to financial incomes and perhaps supplemented by a transfer tax or stamp tax on individual notes and bills, the concentration of taxation which comes from taxing the *res* and at the same time the *debitum* would be largely avoided together with the injustice that is sure to follow such concentration. But care should be taken that the income tax should not be restricted to stocks and bonds but should bear on all sorts of credits.¹ The difficulty connected with mortgages was so much felt in France that they were exempt from taxation there.² It would be possible to exempt farm mortgages.

The great iniquity of our American system of state administration is that assessors are political and irresponsible. The tax is really laid arbitrarily by the assessor in face of the rate enacted by the legislature or by the tax commission, as the case may be. The assessors really make the rate by estimating the principal at their own sweet wills. It is true that the district assessors taken alone are not entirely arbitrary. Their assessments are reviewed by county boards, and the county assessments are reviewed by state boards. But the system

¹ Leroy-Beaulieu, *op. cit.*, pp. 421-422, 418.

² *Ibid.*, 420.

is one leading to a progressive lowering of assessments. In this respect it is thoroughly democratic. One is reminded of the tremendous pressure in an advanced democracy (as in an extreme autocracy) to lower the standard of value — the inflation craze. Happily cheap money has been counteracted by the influence of the business classes. It is to-day's duty to confront the problem of cheap assessments. "But the climax of absurdity is reached in the metropolis of the West. The city of Chicago has the reputation of never doing things by halves; 'when it is good it is very, very good and when it is bad it is horrid.' There the process of juggling with tax rates and tax assessments has been carried to the point where the results are truly horrid. It is common in Chicago to value real estate at $\frac{1}{4}$ or $\frac{1}{10}$ of what it would really sell for and then to tax it at an apparently exorbitant rate on this unblushingly mendacious valuation. Hence we find a nominal tax rate of \$80 to \$100 on each \$1000 of property. The processes by which this absurd result has been reached we cannot stop to unravel, and fortunately it is in the main of purely local interest. But obviously no citizen who conformed to the letter of the law in Chicago could possibly afford to own any sort of security; for at the lawful established rates he would be called on to pay annually in taxes much more than his investment could yield in income. The epigram of Judge Lowell here falls short of the literal truth: 'In Chicago taxation is outright confiscation tempered with outrageous favoritism.'" ¹ Democracy is continually impelled to hoist itself by its own petard. In its attempt to regulate everything in popular interest it is thrown constantly into the arms of Arbitrary Benevolence. But sometimes it misses Arbitrary Benevolence and falls into the lap of Persevering Mischief; Enlightened Self-Interest is, by and large, the most competent to save the situation, but finds her hands tied in many questions that are unavoidably political. In these exceptional but important cases Expert and Professor obtain a hearing along with Experienced Statesman.

Professor Taussig further says: "The maxim that the people

¹ Taussig (F. W.), "The Taxation of Securities in the United States," in *Political Science Quarterly*, Vol. XIV, p. 111.

should rule has led to the practice, so common in our political system and so unfortunate, in many of its results, of electing directly by popular vote any and every popular officer from the state governor to the town constable. In the opinion alike of scholarly investigators and of sagacious statesmen, popular government would be vastly better and more efficient if the number of elective offices were reduced to the minimum. Yet this means of improving popular government is often thwarted by the very strength of the democratic tradition, which is the foundation of popular government. And similarly the strength of the healthy tradition that all should pay taxes in proportion to their means stands in the way of effective measures for securing the best approximation to that admittedly desirable end."¹

A special tax is one the proceeds of which are devoted to a particular purpose. An example is where a barbarous nation mortgages its customs revenues to the payment of a national loan, or where a city lays a special rate to defray the expenses of the water service. In a modified sense, we speak of a special tax as a peculiar tax, entirely distinct from others, although the proceeds are paid into the general fund. In this case the specialization partly consists in the employment of a distinct set of agents for the assessment of the tax. These agents are specialists in the assessment of the class of property which alone they are deputed to evaluate. If, for example, the property tax were to be transformed into simply a land and house tax, the task of the assessors would be greatly simplified, notwithstanding the objection that the lands and houses used for residence or refined living have no capital value in any economic sense. But the same assessors might be wholly incompetent to evaluate house furnishings. I know a case of a family in very moderate circumstances in whose tasteful little home are hung a large number of attractive but cheap pictures. The assessor was much impressed with the value of these pictures and shoved up the assessment out of all proportion to the means of the contributors. If the State is bound to assess such things, it should send a specialist to do the work, putting a separate tax on household goods. As a matter of fact, the central

¹ Taussig (F. W.), "The Taxation of Securities in the United States," in *Political Science Quarterly*, Vol. XIV., p. 111.

authorities do separate the property tax into several classes of objects, all assessed, however, by the same deputies. But, as if to make comparison impossible, and perhaps comparison is not desired, they change these classifications from year to year.

It is clear from the example of unjust taxation cited, that a more uniform and just result for each taxpayer would be reached by means of a differentiation of the duties of the assessors. In that case each assessor would evaluate fewer objects and would cover a wider area. The work could probably be done by a smaller corps of deputy assessors than that employed at present. When it comes to assessment of certain corporations and credits, the bad logic of the blanket assessment plan has been so glaring that the States have already in many cases established separate boards for them.

On the other hand, excessive specialization of taxes is admittedly a bad thing. It tends to excessive specialization of the machinery of assessment and collection. However, excessive uniformity of taxation is unpractical. One of its worst features, as already mentioned, is a crude employment of the same agents of administration for different kinds of work. The abuse would not perhaps be so bad if the assessors were the agents of the central governments of the several States, holding office under civil service rules; but local assessors, locally elected, are naturally more under the influence of their constituents than of the revising boards. Their fealty is primarily to the party to which they belong; their object is to make their party locally popular; and progressive decrease of assessment is the inevitable result.

In England the land tax and house tax, the income tax, the excise tax and the death duties all go to the general treasury; but, in the nature of things, they must be collected by separate officials. The income tax, indeed, is provided with a central administration partly separated from that of the other taxes; and again, its various schedules (at least schedule D) are separately assessed. "Schedule D includes the income from trades, professions and business, from colonial or foreign possessions, from the stocks or bonds of colonial or foreign cor-

porations, and from any other sources which are not specifically included in any other schedule."¹

The borough, county and poor rates are devoted to local objects, and collected by entirely distinct officials from those for the national taxes. The poor rate is indeed the basis of the other local taxes, such as the borough rate, the watch rate, the lighting rate, the sewers rate and so forth. These taxes are added on to the same basis, just as we add the State, county, town, school, university and other rates on to the property tax.² And yet no one in England complains of "double taxation" on this account.

In France, on the other hand, all taxes are collected by a centralized administration. But evidently separate officials must be assigned to such diverse objects as the assessment of the *octroi*, of the various taxes on realty, of the taxes on records, of transfer of property, including probate, of the stamp duties,³ of the taxes on playing cards, etc.,⁴ of the taxes on businesses and professions, on corporation profits, on stock exchange transactions, not to speak of the customs duties. Some of these taxes, *e.g.* land and business taxes, are fixed in rate by ancient legislation, and are made to bring in a bigger revenue, at times, by the *centimes additionels*. And yet no one in France accuses the state of "double taxation" on this account.

In the case of the property tax, we have multiplicity of taxes without the advantages of multiplicity, — for the property tax hits each man but once (or misses him), and hence is so far a single tax on him. It is really "double" taxation because it is the most unequal taxation. Greater equality is obtained by a multiplicity of taxes, many of which hit one person, but in such unequal degree that an average is struck which produces greater equality and hence avoids "double" taxation: if one tax hits the individual too much, another hits him too little. In fact, it is only under multiplicity of taxation that the holder of credits is reached, and that holders of different

¹ Hill (J. A.), "The English Income Tax," in "Economic Studies," Vol. IV, Nos. 4 and 5, "American Economic Association," 1889, p. 262. The very interesting details of the appointment of the "General Commissioners" and of the assessors and clerks, are given in Ch. III, "The Machinery of Assessment."

² Leroy-Beaulieu, "Science des Finances," p. 713.

³ *Ibid.*, p. 515.

⁴ *Ibid.*, pp. 426, 632.

credits can be reached at all fairly. It is true that the private money-lender is hard to reach, but still stamp duties on notes and bills will reach him if they are not imposed also on corporations. And a tax on the recording of mortgages will also reach him. Perhaps mortgages should be exempt until a general agreement among the States as to them can be reached.

Professor Le Rossignol suggests that a preliminary move in the right direction would be to double the length of the term of office of the county assessors. They would be encouraged to make more independent valuations.¹

It is not the business of the reformer to redress inequalities of fortune, but inequalities of taxation. A slightly progressive tax on large incomes and large credit returns is permissible since the consumption of the rich is less proportionally to their fortunes, for they contribute less to the excise, license, customs, internal revenue and other direct taxes than the poor. Multiplicity of taxation allows each separate tax to stand at a very low rate, and hence the injustice that is inherent in each tax is minimized. This system of many light taxes interferes least with free individual enterprise. Human sense of justice is satisfied by the feeling that one's lot has been settled in a free contest of personal powers in an open field of free competition. It is interference with the industrial contest that arouses indignation, whether that interference comes from the violation of the ethical rules of the commercial game on the part of the employer or from the arbitrary requisitions of the taxgatherer. Any single tax, especially one that has the pretension of taxing a theoretical "social surplus," gives loose rein to arbitrariness. It is found to break up into a series of different, uncanonical taxes.

¹ "Taxation in Colorado," p. 63.

TAXATION OF MONEYS AND CREDITS

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IN the consideration of the subject "Taxation of Moneys and Credits" I have taken the Iowa definition as a basis. In Iowa the term, "moneys and credits," includes stocks, bonds, notes, mortgages, accounts and all evidences of debt.

Widely divergent views and widely divergent policies prevail in this country in regard to the taxation of these debt obligations. In some few States none are taxed, in many an effort is made to tax all and in others some plan between these extremes is in existence.

The general property tax, or the system of trying to tax all wealth and all evidences of wealth, was adopted in this country when it was first settled, when practically all of our wealth consisted of real estate and tangible property. Under those conditions a general property tax was a satisfactory system of taxation.

But with the industrial and financial development of the country, the organization of corporations of all kinds, and the growth of our national system of credits an entirely different condition developed. Many people invested in the stocks or the bonds of the corporations and in the notes and mortgages of the landowners. These certificates were almost universally held to be property and an effort made in almost every State to tax at least some of them. Legislatures declared stocks, bonds, notes, mortgages and all evidences of debt to be property, and stringent laws were passed in an endeavor to place the same on the assessor's books for taxation.

It has taken years of education to convince even a few of our people that the general property tax is wrong in theory, and impossible of enforcement. In the past few decades, however, there has been a tendency toward the adoption of special taxes for special purposes. Several state constitutions have been

amended to allow the legislatures more power in the matter of taxation. This has resulted in the adoption of improved systems of taxation in some of the States; and the disposition is very marked at this time toward the adoption of improved systems of taxation that are sound economically and possible of enforcement.

STOCKS AND BONDS

It is a commonly accepted theory in most States that shares of stock issued by a corporation are property or wealth and should be taxed. But that this is an erroneous idea is clearly shown by a simple illustration.

A man with ample means builds, equips and operates a railroad as a private enterprise. He is taxed on the entire value of the road, on its roadbed, its equipment, and franchise values. That is his entire tax. He is not asked to give in for taxation the money he has invested in the road, in addition to the road itself. The property, the wealth, is taxed and that is all.

For some one of a hundred reasons he decides to sell part of the road and forms a partnership with several other men, each owning an equal share. For convenience they turn the management of the road over to one of the partners, and the others only meet once a year to check over business. The same rule of taxation still applies, and the property is all that is taxed. The individual partners are not expected to pay a tax on their investment.

In the course of time some of the partners sell parts of their shares to other persons. The interest owned by the different ones becomes varied, a large number of persons become partners. It is difficult to tell just how much of the profits belong to each or how much of a voice in the management of affairs each should have. For convenience it is decided to form a corporation and give each partner shares in the corporation equal to his interest in the partnership. This is done, and immediately a new plan of taxation is encountered. In addition to the property owned by the individual, by the partnership and now by the corporation, it is insisted by many that the shares of stock should also be assessed, that they are property, that they are wealth.

Bonds issued by private corporations are subject to the same conditions as the stock. The only difference is that the bondholder is granted some rights not enjoyed by the stockholder and is denied some privileges granted to the stockholder.

A consideration of the cause of a bond issue will show these facts. A bond issue is, or should be, made for the purpose of taking up a floating debt contracted in the transaction of the business of the corporation, or for the purpose of enlarging or improving the business. In either case the stockholders desire to retain control of the property, and in order to do this are willing that those becoming partners and furnishing the additional money shall be guaranteed a fixed interest on their investment, with the further advantage that if such interest is not paid, that then the bondholders have a right to take over the property as owners, with the consequent loss of their interest to the stockholders.

On condition of the partners owning bonds accepting a small fixed rate of interest, with no share in additional earnings or in the control of the property, they are given in return for these concessions by the partners owning stock a guaranteed return and a first lien on the entire property.

Such an arrangement could be made between two partners, and no one would advocate taxing their interests in the property in addition to the property itself.

The bond issue is a simple way of making such an arrangement, and in large issues a means of dividing up the part represented by the bonds into amounts to suit the different investors.

Those who favor the taxing of stocks and bonds must believe that somewhere between the time that the partnership ceased and the time that the corporation began business as such, an amount of property, of wealth, was legislatively created equal to the original amount. This conclusion cannot be established by any possible system of reasoning. The fact is, the only thing that has been created is the sheets of engraved paper showing just what share of the total property is owned by each stockholder and each bondholder.

The same rule holds good even if the stock and bonds had been issued when the road was first built. Instead of one man

furnishing the money, a number of men put in different amounts, and the stock and bonds issued to show the share owned by each.

Take any corporation and there would be no loss of property if all the stock and bonds were retired and the corporation changed into a partnership, or individual ownership.

While stock in a corporation is in no sense wealth or property, and should not be taxed as such, there are certain special advantages granted to corporations, by the State, that are of great value, and these special privileges should be subject to a special tax. A corporation can more easily transfer a share of its property by the use of stock, it has a fixed succession, very often the stockholders or partners are relieved of any further financial obligation in case of failure, it simplifies the organization, and the State often exercises a supervision over the business. These and many other advantages are granted by the State to corporations, and in return for such special privileges, the corporation, as such, should pay a small annual fee to the State. Those States that have adopted this policy have solved the question of the taxation of stocks.

This tax should go entirely to the State as part of the state revenues, as it is the State that grants the special privileges enjoyed.

Bonds also have certain advantages over other evidences of property rights. They usually run for a long term of years, are easily transferred and have a ready market value. They should be subject to a small special state tax in return for the special advantages granted by the State. The tax should be paid by the corporation, because, on account of these special privileges granted by the State, the corporation is able to secure additional capital at a lesser rate of interest than can a private person or a partnership.

When the business of a corporation is limited to one State, the entire license tax should go to that State. In the case of corporations doing an interstate business, a report should be required by each State in which the corporation does business. The stock and bonds should be prorated among the different States in proportion to the capital or property used in each State.

It would be unfair for each State to require a corporation

doing an interstate business to pay a license tax on its entire stock and bond issue, as in that case a corporation doing business in a large number of States would be subject to a prohibitive tax. But on the contrary each State is entitled to a reasonable license for the privilege granted to the corporation of transacting business in that State.

Alabama, New York, Ohio, Oregon and other States have adopted the license tax in one form or another. In some, as in Ohio, the tax is a certain per cent of the capital stock. The Ohio tax is $\frac{1}{10}$ of 1 per cent with a minimum of \$10. In other States, as in Alabama, it is a fixed sum for different amounts. In Alabama it varies from a minimum of \$10 on all corporations capitalized for less than \$10,000 to \$500 for those capitalized for over \$1,000,000.

Foreign and domestic corporations should be taxed at the same rate, and the rate, or plan, should be the same in the different States.

The California commission recommended that all corporations, irrespective of size, be taxed on the same basis, and fixed the amount at $\frac{1}{10}$ of 1 per cent. This is preferable to the Alabama plan, although in fact most States tax the larger corporations less in proportion than the smaller ones. If the tax is the same on all corporations, irrespective of size, it will do much to cure the evils of overcapitalization that have recently caused so much trouble in the financial world.

PUBLIC BONDS

Bonds issued by cities, towns, counties and other municipal and political corporations should never be taxed. Any tax to which such bonds are subject is added to the interest rate, and comes directly from the taxpayers. The taxpayer is required to pay interest on the theory that the bonds may be taxed, but in fact the bonds are seldom entered for taxation.

If municipal bonds were exempt from taxation, the municipalities could usually sell their bonds at home. It would then be possible to offer the bonds at popular subscription and there would be a great saving in the interest rate that such corporations, or in reality what the taxpayers, are required to pay.

MORTGAGES

Many States attempt to tax mortgages in addition to taxing the property covered by the mortgage. The plans adopted vary in detail, but all are failures in practice.

Under the general property tax the only mortgages that are taxed are those made on land in the immediate vicinity of the home of the owner of the mortgage. Mortgages owned outside of the State, and often even outside of the county in which the property covered by the mortgage is located, are seldom taxed.

In some States the extreme theory prevails, that the mortgage should be taxed only where the owner resides. This in practice offers a premium to a citizen of those States to send his money out of the State for investment in order to escape taxation, and gives to the foreign capitalist an opportunity to make the necessary loans, and he also escapes taxation.

Statistics issued by the New York Tax Reform Association show that where mortgages are subject to taxation, the increase in interest rates covers the entire tax liability or risk.

Prior to 1905 mortgages were taxed in New York, the same as other personal property. As in all cases, where such a policy is in force, only a small per cent of the mortgages were actually taxed, but the interest charges were loaded about one half of one per cent, to cover the tax risk.

In the neighboring State of Massachusetts, mortgages were not taxed as such, and comparisons made between Massachusetts and New York proved conclusively that the tax liability was covered in the interest charge.

In the city of Boston the average rate of interest was 5.03 per cent, in New York City it was 5.18 per cent and in Brooklyn 5.27 per cent. In two Massachusetts counties containing no large cities the interest rate was 5.56 per cent, while in six similar New York counties the interest rate varied from 5.88 per cent to 6.12 per cent.

If it were not true that the tax risk is added to the interest charge, the rate of interest would have been lower in New York than in Massachusetts, as money is cheaper in New York than in Massachusetts.

The interest rate in New York, under the different systems of taxation, also proves that the borrower pays the tax.

Under the general property tax, when few mortgages were given in for taxation, the average mortgage interest rate in New York City was 5.12 per cent.

On July 1, 1905, a law went into effect in New York taxing mortgages fifty cents per annum for each one hundred dollars or major fraction thereof, a much less rate of taxation than on other property, and yet the mortgage interest rate increased in the next year to 5.54 per cent, a net increase of .42 per cent, an amount nearly equal to the entire tax.

On July 1, 1906, the system was changed to a recording tax of fifty cents per hundred or major fraction thereof to be paid only once. Under this plan the mortgage interest rate decreased to 5.15 per cent, and this, too, in spite of the fact of an unusual stringency in the money market.

• In Minnesota, where a mortgage recording tax displaced the general property tax in April of this year, there has been a reduction in interest rates of from nearly one half of one per cent in the cities to approximately two per cent in the small towns and villages.

Hon. Frank Clague, Senator from the 19th Minnesota District, who had charge of the bill enacted in that State, says in a recent letter:

"I am fully aware that the borrower will have to pay the tax. I knew this before the bill was introduced; but even if the borrower does pay the tax, I am thoroughly convinced that it will give the borrower in the end cheaper interest. In the little village where I live money can to-day be borrowed for 2 per cent cheaper on village property than it could prior to the passage of the law. This is due to the fact that most of the loans which are made on village property are by local parties. Under the old law it would cost the owner about 3 per cent tax on the loan annually."

Get the fact plainly before the people that the borrower pays the tax and the greatest prejudice against the change from the general property tax is overcome. The average borrower of money believes that the man from whom he borrows pays the tax; but let him be convinced of the true state of affairs,

of the fact that he pays the tax on the mortgage, even if the capitalist escapes the tax by offset or false statements, and an influence will be exerted that will soon result in the exemption of mortgages from the general property tax.

A tax on property, and a tax on a mortgage against that property, is double taxation, and the owner of the property pays both taxes.

If a man has property valued at \$10,000, but mortgaged for \$5000, he has in reality only a \$5000 interest in that property, but he is assessed for the full \$10,000 and pays taxes on that amount. He pays the taxes on the \$5000 mortgage by paying an increased interest.

Several plans have been tried to relieve this double taxation.

In Wisconsin, California and some other States it has been provided that the amount of the mortgage shall be deducted from the assessed value of the real estate, and that either the owner of the real estate, or of the mortgage, shall pay the tax. This is a great improvement over the general property tax as it does away with double taxation.

Another plan is the one now in force in New York and Minnesota, and known as the Mortgage Recording Tax. This plan provides for a tax of fifty cents on each one hundred dollars or major fraction thereof, to be paid when the mortgage is recorded and paid only once.

In New York the first reform secured was a law providing for an annual tax of fifty cents per one hundred dollars, but after a two years' trial the law was again amended and the recording mortgage tax adopted.

In Minnesota it was necessary to amend the constitution before the law could be changed, but it was done, and last winter the law recommended by the New York Tax Reform Association was enacted in that State. In the letter from Hon. Frank Clague above quoted, he further says:

"Under our law as provided by Sec. 2, a tax of 50 cts. per \$100 is paid when the mortgage is placed on record. It matters not whether the mortgage is for one day or ten years. The tax of 50 cts. per \$100 has to be paid. This arbitrary rule does in certain cases no doubt work an injustice, particularly where the mortgage runs for a very short time. This matter was discussed

very thoroughly by our committee before the bill was put out for passage. It is a copy of the New York Law as to tax charged and as to time. It appears to work well in New York and in Alabama, where it has been in force for several years. I am satisfied the law will be a success here. Some changes will need to be made, which can only be worked out in practice. I am inclined to believe that a more just tax, or rate, would be as follows:

10 cts. per \$100 for 3 years or under.
20 cts. per \$100 for 3 years or over.

The banks of our state opposed the law very generally before its passage, on the ground and for the reason that they believed it would greatly injure deposits. For the short time that it has been in operation the banks now appear to be satisfied with the law. It has not to any extent affected the deposits.

"It will be a source of great revenue to the different counties. It is estimated that in Hennepin County, in which the city of Minneapolis is located, it will produce \$140,000 annually. Ramsey County, where St. Paul is located, the estimate is about \$100,000. Under our law the money goes to the counties. All mortgages renewed will have to pay the tax."

Delaware has entirely exempted mortgages from taxation, with the result that mortgage interest rates have reached the lowest figure in that State.

Mortgages should not be taxed as property as they in themselves are not property.

When the owner of property mortgages it, he in reality sells an interest in it to the mortgagee. As in the case of the owner of bonds issued by a corporation, so the owner of the mortgage is willing to allow the mortgagor control of the property and to retain all the profits above a certain amount on condition that the return of interest on his share shall be secured, and in case that the owner, the active manager of the business, does not make a success of the same that he then can take possession. The same result could be secured by a partnership contract. but it would be more cumbersome, and not so easily enforced. The State has simply provided an easy way of carrying out such a partnership by means of a mortgage. In return, however, for the special advantages granted mortgages by the State it is just to exact a reasonable pay for these special advantages.

The mortgage recording tax of New York and Minnesota meets this condition. Such a law is even better than complete exemption.

It overcomes every objection that can be raised to the general property tax. It places the home money lender on an equal footing with the foreign money lender; it is easy to enforce and simple in its workings. It charges for the special privileges granted by the State.

In actual practice the result seems to be that in consequence of foreign mortgages being required to pay the tax, it actually increases the revenue derived from mortgages, while greatly reducing the burden imposed on domestic capital.

UNSECURED EVIDENCES OF DEBT

Notes, accounts, deposits and other unsecured evidences of debt are subject to taxation in almost every State.

Every argument in favor of exempting stocks, bonds and mortgages from taxation, applies with even greater force to all unsecured evidences of debt.

A bank deposit drawing interest represents an interest in the bank. The depositor is given the security of the bank's capital, with a dividend on his share in the business guaranteed, and in return for these guarantees is willing to accept a small return, and to allow the stockholders all the profits over the guaranteed return.

Money borrowed on a note is usually put into property of some kind. The owner of the note has an interest in all the property of the borrower but is not secured by the pledge of any particular items. But if his interest is not forthcoming, he can insist on it, and all the property of the borrower, except such as is exempt by law, can be taken to secure his interest and his original investment.

Efforts have been made, and some results secured, in a number of States to reform the law relating to taxation of secured credits, but for some unexplainable reason no results seem to have been secured in any State, except Delaware, to exempt unsecured credits from taxation.

In New York, Massachusetts, Minnesota and other advanced States efforts are still being abortively made to tax this class of credits.

In California the commission, after finding these unsecured debt obligations as not in any sense property and not suitable subjects for taxation, and presenting their reasons for so finding in the strongest possible language, advised that the old rule be retained and no effort made to secure relief at that time for fear that it would confuse the main issue, which was the separation of state from local taxation.

This strange condition is hard to explain. If stocks, bonds and mortgages that are more or less subjects of public record ought not and cannot be located for taxation, how much more is this true of those other evidences of debt that can be carried in the pocket or deposited in a safe and no one but the owner and the debtor know of the transaction.

DEDUCTION OF INDEBTEDNESS

In every State where an effort is made to tax one or more classes of moneys and credits, the law provides that the owner of such moneys and credits may offset the same by any indebtedness owed by him. In a few States it is provided that only such debts may be offset as are actually owed residents of the State.

This is one of the most unlogical provisions of our tax laws. If these credits are suitable subjects for taxation, then they should be taxed. There is no more reason for allowing an offset on these credits, if they are to be taxed at all, than to allow an offset on property of every kind. If moneys and credits are to be taxed at all, then they should be placed under the same conditions as all other taxable property.

The very fact that legislatures have uniformly passed laws providing for the offset of moneys and credits by indebtedness is an indication that they were not sure in their own minds that moneys and credits should be taxed at all.

In practice, this provision for offsetting credits by debts is the cause of a large share of the trouble of the assessing bodies and of the misrepresentation by the citizen. It is no relief to the man of small means because such a man, if he has any money, will immediately pay his debts. It is a benefit only to those capitalists who, on the one hand, have large credits, and on the other may, for the purpose of taxation, accumulate large debts.

A merchant can very easily, immediately preceding the date of assessment, buy large quantities of goods for future delivery. He has created the debt necessary to offset all his moneys and credits, and the goods, not being delivered until some future date, are not in his possession when his assessment is made.

The financier who has large credits can easily owe an equal amount on real estate owned by him ; and in practice this is what he usually does.

This offsetting of indebtedness results, as a general thing, that the only citizens who pay taxes on moneys and credits are the workingman who has accumulated a few hundred dollars, the executor of some estate, or the widow who has a few thousand dollars, on the income of which she must live.

RESULTS OF TAX ON CREDITS

In judging of the probable success of any plan to tax moneys and credits there are certain facts or conditions that must be considered.

The greatest and most important of these facts was forcibly if not elegantly stated by the great psalmist when he said, "All men are liars." That statement was true in the times of David ; it is true to-day, and it will be true a thousand years in the future.

The same truth is expressed in academic language by a professor of economics in Edinburgh University in the following words: "It may be observed that in practical politics it is generally taken for granted that a tax that can be evaded will be evaded."

It may be true that there are many who will not lie for a dime or a dollar, but if the incentive is strong enough, if the benefit to self is large enough and the chance of being found out is small enough, there is probably no one in the whole world who will not lie.

It certainly is true that the Christian religion, that can reform the drunkard and the thief, that can lift a man from the depths of degradation and win him a place among his fellows, cannot raise him to a plane of virtue so high that he will honestly give in his credits for taxation. There may be exceptions, but hardly enough to prove the rule.

This condition prevails in spite of the admonition of the Great Teacher, who said, "Render to Cæsar the things that are Cæsar's, and to God the things that are God's," or according to the twentieth-century edition of the New Testament, "Pay to the Emperor what belongs to the Emperor, and to God what belongs to God." This statement was made in reply to the question as to what should be done with the demand for tribute, or in other words what should be done with the assessor and the tax collector. The first command was to pay the taxes demanded by the State. And yet we all know many a good man who will go to any length to escape the taxation of his moneys and credits and then cheerfully give the tax money thus saved by his lying and perjury to his church.

Any governmental policy that corrupts our political conscience, that makes liars out of our people, that puts a premium on perjury, that places a penalty on honesty, that is almost universally evaded, that is evaded by and with the assistance of public officials and that cannot be enforced even with the most drastic penalties, is a bad policy and should be repealed.

That the policy of taxing or trying to tax moneys and credits does these things no one will deny. In every State the law taxing moneys and credits is held in utter contempt. No one is expected to comply with its provisions.

The California Commission uses these words in speaking of the assessment of moneys and credits:

"Our present system is a school for perjury, it puts a penalty on honesty and pays high premiums for dishonesty. The burden of the support of the government falls most unequally upon those who should bear it. It falls with special severity upon the poor and with the greatest severity upon the honest. It is highly conducive to political immorality and is a veritable school for perjury."

It is equally true that the law is generally evaded and that too with the consent and assistance of those officers whose special duty it is to enforce the law. The per cent of moneys and credits given in for assessment is ridiculously small in every State. In California, in 1906, the moneys and credits comprised only 2 per cent of the entire assessment, and included in this was the surplus

credits over deposits of the banks. In Wisconsin, in 1903, the moneys and credits comprised only 5.33 per cent of the entire assessment, and this included all mortgages. The per cent of moneys and credits given in for assessment is equally small in all of the States.

The officials whose duty it is to assess moneys and credits seldom try to discover just what the citizen has. It has well been said that the assessment of credits is on the same principle as a Sunday school collection, that the free will offerings are thankfully received, and no questions asked.

The prosecuting officers are equally negligent in enforcing the laws regarding assessments. The public demand that the drunk be sentenced to jail, that the thief be given the full penalty, that the poor and the ignorant who make up the petty offenders be prosecuted to the limit of the law, but there is no demand for the prosecution of the prominent and good citizen who violates the assessment laws and is, under the law, much the greater criminal.

Different States have endeavored to secure the return of moneys and credits for assessment by the passage of the most drastic laws. Iowa is a fair example of this condition, but the laws are similar in all the States. Under the law every person when being assessed must subscribe to an oath or affirmation to the correctness of his assessment. Any one who knowingly or willfully makes a false statement in his return to the assessor is deemed guilty of perjury, and the penalty for perjury in a case of this kind is fixed at imprisonment in the penitentiary at not more than ten years. No law could be more simple or more easy to understand. It would seem that under such laws no one would dare to make a false return; but the fact is that the law is violated thousands of times each year, and while the tax ferrets have discovered thousands of false returns, there has not, in the ten years that these laws have been on the statute books, been a single prosecution started under them.

Where one law is universally violated it is a well established fact that this tends to create a contempt for all laws. It is not strange that when important criminal statutes are thus violated with impunity by our leading citizens, by our prominent business men and by our active church members, that the petty thief

or the common drunk cannot understand why he should be made amenable to the law while his more fortunate neighbor enjoys the fruits of his violation and no one dreams of starting criminal proceedings.

When the direct commands of the Great Teacher, and the severe penalties of the civil law, fail to make an appreciable per cent of the people comply with the provisions of a law, there can be only one reason therefor and that is that the law is fundamentally wrong. This is certainly the only explanation that can be made and it is the true one. Irrespective of the fact that legislatures have declared one or more of the different classes of moneys and credits to be property and fit subjects for taxation, the people feel deep down in their consciousness, even when they have not given the subject any great consideration, that the legislatures have made a mistake, that moneys and credits are not property, that they should not be taxed.

The Wisconsin Tax Commission uses the following words in relation to the taxation of credits. "Laws which are fundamentally wrong are incapable of substantial enforcement among free and enlightened people; and the fact that the assessment laws under discussion have never been effectually enforced is evidence that there is some radical defect in the principle upon which such laws are founded. It would not be wholly correct to assert that in their practical rejection of such laws the people and their assessors have shown themselves wiser than their lawmakers; but is it not true that by instinct or intuition they have arrived at correct conclusions which have not as yet been consciously perceived by the majority of legislators?"

The argument is often made, and with seeming justice, that because the law in relation to the taxation of moneys and credits is violated, is no more reason why it should be repealed than that because some commit murder, the law against murder should be repealed. The conditions, however, are in no way similar. All our citizens believe in the enforcement of the laws against murder, the great majority do not violate these laws, and all cheerfully coöperate in their enforcement. But with the law for taxation of moneys and credits, few believe that it should be enforced, the vast majority of those who have credits violate

the law, and few, if any, of our citizens are willing to coöperate in its enforcement.

There is all the difference between a criminal statute that is usually enforced and one that is never enforced. Any law that is a dead law should be repealed.

Another great objection to the exemption of moneys and credits from taxation is based on the false assumption that if all notes, mortgages, stocks, bonds and other credits are exempted from taxation, that our wealthiest citizens who have the greatest share of their wealth represented by these will entirely escape taxation. This, however, is not the case. If all the property of the corporation is assessed for taxation at its full value, all the wealth represented by the stocks and bonds is taxed. The tax must, then, be paid before interest on the bonds or dividends on the stock. If the property itself is taxed, the stock and bond holders who own the property pay the tax just as surely as if the property were owned by one person.

In the case of notes and mortgages the borrower always pays the tax in the increased rate of interest he is compelled to pay. If these credits were exempt, the interest rate would be just so much less.

The fact should always be remembered that stocks, bonds, mortgages, notes and other evidences of debt are not property, but just so much paper, containing certain words, showing the holder's exact interest or share in some particular property, and that these forms are adopted on account of their simplicity. In every case the stocks and bonds, or the notes and mortgages, could be replaced by a partnership agreement and the same amount of property would be represented as before the change. Admitting that individuals or partners should not be taxed on their investment in addition to their property, the conclusion must be reached that moneys and credits are not property, and should not be as property subject to taxation.

REFORMS

In order to change from the general property tax to a system of taxation of moneys and credits that is reasonable and that can be enforced, a number of changes are necessary.

1. In those States where the general property tax is embodied

in the state constitution, it is necessary to secure amendments to the same, allowing the legislature greater freedom in the matter of taxation. The best plan is to leave the matter of taxation entirely to the legislature as changing conditions can then be met with much less trouble.

2. To do away entirely with the deduction of indebtedness from moneys and credits.

If it is impossible to secure a law doing away entirely with exemptions, such deductions should at least be limited to debts owed residents of the same State, and if possible to only such debts as are assessed for taxation.

The repeal of this provision would greatly simplify the question of taxation of moneys and credits as it would then be considered entirely on its merits.

3. All unsecured evidences of debt, all such credits that are not required to be made a public record, everything in regard to which it is necessary to depend entirely upon the owner for information, should be absolutely exempted from taxation. So long as people are constituted as they are to-day, — and that will be until the end of time, — it will be utterly impossible to compel them to give in for taxation their property that can be concealed.

4. Mortgages should be taxed by a mortgage recording tax to be paid only once. The New York and Minnesota plan meets the requirements of a tax on mortgages that is fair to the citizen and to the State. If this plan cannot be secured, then the Wisconsin and California plan of deducting the amount of the mortgage from the assessed value of the property should be adopted. The plan of double taxation under the general property tax should not be allowed in any case.

5. Stocks and bonds should be exempt from taxation and made subject to an annual license or franchise tax, the same to go to the State. The property of the corporation should be assessed at its full value and the aggregate market value of all stocks and bonds should be considered in fixing the value of the property.

6. For general taxation only those things that can be seen, that can be located by the assessing body, should be assessed for taxation.

7. The personality of the taxpayer should be eliminated from the assessment. Property as such should be assessed and not the individual. The assessor should in every case fix the value of everything that he assesses and in no case should the citizen be required to place a value on his assessable property.

If these reforms can be secured they will do more to solve the present problems of taxation and do more to improve our political morals than will any other reform that could be suggested.

FARM MORTGAGES AND DOUBLE TAXATION IN VERMONT—SITUATION AND REMEDY

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THE situation in Vermont with respect to double taxation of encumbered real estate, through the taxation, or rather attempted taxation, of mortgages is as follows:

Mortgages, other than those held by the banks, are supposed to be taxed like other intangible personal property. The average local rate throughout the State is about one and one half per cent. The banks pay, in lieu of taxes on their mortgages, seven tenths of 1 per cent on their deposits. The mortgages held outside the banks are, indeed, taxed "like other intangible personal property"; that is to say, by far the greater part escape paying the tax altogether. In those cases where the mortgagees are caught (by reason of a tender conscience mainly, such are the loopholes available), of course they do not really *pay* the tax (except occasionally in part), they only advance it. They act virtually as agents for the tax collector, and shift the tax burden to the mortgagor when new loans are made or old ones renewed. At this point it is necessary to introduce some economic theory, as constituting really a part of the description of the "situation."

It is well known to students of financial affairs that a lender expects, under given economic conditions, to make a certain per cent net; and that he does make it on fresh loans, and is content with it as being his true "interest" on the money advanced. The gross interest paid by the borrower and received by the lender, whenever any particular class of loans are taxable, is in part not real "interest" but *compensation for the tax* if paid, or a *premium for risk* if it is not paid. Of course when the lender's gross receipts of interest are fixed in an old, standing loan and a new tax is imposed, he cannot shift the tax during the life of that loan, but really pays it himself. Again, if on

fresh loans he pays a tax higher than others pay on the same class of loans, naturally in that case also he is burdened as long as he stays in the market under these conditions. On the other hand, if he makes fresh loans, paying habitually a less tax, or running a less risk of paying, than others do in the same class, he will enjoy a positive bonus; he will reap an advantage from the gross interest rate created by the general situation. Considering lending as a continuing performance, and having regard to the average lender, we may say definitely that a tax on a loan is never really paid by the lender but is always shifted to the borrower. In such cases, in short, the taxpayer is not the tax bearer. These truths are universal: now let us return to the facts in Vermont in particular.

The savings banks and trust companies of the State, by reason of paying out of their gross interest only seven tenths of 1 per cent, have the "pick" of the loans secured by mortgage. Borrowers who deal with private lenders are, on the whole, a separate class with credit not of the first rank. The lenders upon mortgage outside the banks, although as a rule they pay no taxes from their gross interest, are under considerable risk of paying; or, rather, a more correct way of putting it would be to say that for one reason and another, enough of them pay to determine the loan market and fix the rate of interest on all mortgage loans. If the legal tax on mortgages were universally escaped, it would obviously be a dead letter and of no effect. It is paid just often enough so that, while little revenue for the towns is obtained, about 1 per cent is thereby added throughout the State to the interest on this class of loans. This interest surcharge, in other words, emerges from the whole situation. The exact amount of it, of course, is a matter of estimate; but I think it a just and conservative estimate that money obtained upon mortgage to develop the rural property of this State costs the borrowers 1 per cent more than it need cost — it costs 1 per cent more than the money market conditions *and* the credit of the borrower in each case call for. As the owner of a mortgaged farm pays taxes without escape upon the full assessed value of his farm, that payment and the 1 per cent extra interest money is what constitutes the so-called "double taxation."

There is another complication in the situation in this State. The farmer who owes money secured by mortgage on his farm, is allowed by law to set off that debt against his personal property, — even the whole of it in case the mortgage is greater than the personal property. Obviously this “set-off” reduces the net amount of burden by reason of double taxation, but does not remove it altogether, except in cases where the personal property is unusually large. In the typical instance the mortgage is about three times the personal property, and therefore there is a gain on a small sum and a loss on a large sum. Another example of a familiar phenomenon, — “saving at the spigot while you are wasting at the bung.” It amounts to a futile attempt to “whip the devil around a stump,” that is all. Nevertheless this set-off of debt against personal property, is a very dear thing to the hearts of many of our farmers. Whenever the legislature seems about to do something about double taxation, this set-off matter is vigorously dangled before their eyes by the assembled lobby of interested persons, and the movement is headed off. Another bugbear paraded before the legislature when, in particular, they show signs of passing a law abolishing all taxation of mortgages is the picture of rich men putting their entire property into mortgages and thus going scot free from all taxation. It is overlooked that rich or poor they escape anyway in respect to a tax existing before a fresh contract of lending is made. They advance the tax (apparently pay it), and then pass it along in the form of higher interest money.

Obviously the thing which should be done by the legislature is to abolish the personal property set-off for mortgage debt, and at the same time abolish all taxation of mortgages on taxable real estate; *to the end that real estate shall bear one tax burden and only one, directly or indirectly, whether it is mortgaged or not.* That is the simplest plan of reform, but it is too good to be practicable. Some legislatures have such slight independence, they are so little in a position of leadership, that they cannot move in important matters until the whole community moves. Apparently in Vermont, not until every man sees through the theory of incidence of taxation and understands thoroughly the indirect way in which mortgaged real estate is burdened twice by the present system of taxation, will the

taxation of mortgages be done away with. This last is a consummation devoutly to be wished, but not to be expected; and, accordingly, some other plan of reform must be adopted under which the *form* is gone through with of still taxing mortgages. The opposition to letting mortgages go *pro forma* free from taxation is, I think, insuperable.

The plan of reform I propose is a collection-at-the-source division-of-equity plan. Let the mortgagors do the advancing of the tax on mortgages and then (in future contracts) legally deduct it from their gross interest money as nominated in the bond. This is the way the income tax on landlords is collected in England. The tenant pays the tax in the first instance, and then tenders the landlord the tax receipt as part payment of his rent. (Of course the gross rent is raised by that amount; for net economic rent, like interest, is determined by economic, not legal, conditions.) To facilitate matters and prevent misunderstanding and lawsuits it should be enacted that no borrower upon mortgage may "contract out" of this arrangement, just as in England employees may not "contract out" of the employers' liability act. Having thus paid the tax on the mortgage for the mortgagee (as the transaction appears to be), the farmer will then pay a real estate tax on his equity in the farm, — that is, upon the value of the farm after the amount of the mortgage is deducted. To further facilitate matters and prevent any economic shock in passing from the present system to the new, the rate on the mortgagee's interest should be uniform throughout the State at one per cent (the estimated present surcharge); and furthermore the mortgagee's equity should be listed and his apparent tax be payable in the town where the real estate is situated.

Thus to illustrate numerically the existing system, the recommended new system and also the simple plan of reform of abolishing all taxation of mortgages on taxable real estate:

Suppose a farmer with a farm worth \$5000, assessed at full valuation, and encumbered with a mortgage of \$3000, upon which the rate of interest is 6 per cent. Suppose further that the basal interest, apart from all taxation, which the credit of this farmer could command is 5 per cent. Finally, suppose that this farmer has \$1000 worth of personal property, and

that the tax rate in his town is $1\frac{1}{2}$ per cent Under the present law his indebtedness eliminates the tax on his personal property, and leaves a real estate tax only amounting to \$75. He pays in interest on his mortgage \$180. Thus his total outgo in interest and in taxes amounts to \$255. But of this last sum \$150 is basal, economic interest, which, being deducted from the total outgo, leaves his total pecuniary burden, *by reason of taxation*, standing at the figure of \$105. The revenue of the town from this farm is only \$75. The farmer's burden is \$30 a year in excess of the town's revenue, because he pays 1 per cent extra interest money needlessly, — thrown away.

Under the collection-at-the-source division-of-equity plan (and with set-off for debt abolished), a farmer situated as we have supposed would pay, first, on his personal property and on his \$2000 equity direct taxes amounting to \$45. Secondly, he would pay \$180 as interest on his mortgage. This is the same gross interest as before; but now \$150 are paid to the creditor in cash and the remainder by the tender of a tax receipt. The \$30 extra interest money (the 1 per cent surcharge upon the basal, economic interest) would be no longer thrown away, but would go into the town treasury. *In form* it is a payment of the tax on the mortgagee's equity, but it all comes out of the farm nevertheless. The total outgo of our farmer for direct taxes and for interest (pure interest and mortgagee's tax) thus amounts to \$225. Deducting the true economic interest from total outgo, we find his total burden by reason of taxation amounts now to \$75. This total burden of taxation resting on the farmer is identical with the sum received as revenue by the town. There is in contrast to the old system no outgo from the farmer's pocket which serves no useful purpose either economic or fiscal.

Finally, to get all the possibilities before us, we may illustrate the simplest plan of reform of all, — the straight abolition of all taxation of mortgages on taxable real estate, — a plan I do not urge for adoption for political reasons solely. Our farmer, under this last system (already in force in some States), would pay as taxes, on his personal property and on the whole value of his farm, at the previously existing rate of taxation, the sum of \$90. He would pay as interest only \$150, for the interest

surcharge would have disappeared. His total outgo would thus be \$240. His tax burden is increased by this plan in the first instance from \$75 to \$90, not because of waste, but because his town now receives an excessive revenue. The whole farm is now taxed at $1\frac{1}{2}$ per cent, instead of part of it at 1 per cent as under the division-of-equity plan. Deducting the revenue needed from the revenue received, we get \$15 per account with this farm, which could be distributed over all the property in the town in the form of a reduction in the rate of taxation. Thus our farmer in the end could have his total tax burden reduced to \$75, the same as it would be under the division-of-equity plan, and \$30 less than it would be under the existing system. But this direct annual saving of \$30 all told, as contrasted with the existing system, does not tell the whole story. Under this last plan of reform, the reduced rate of taxation for everybody would stimulate the growth of the town, and eventually would cause the value of all its property to increase, including the farm we have been considering. Not only would the town be a better place for improving farms with borrowed capital, but all forms of business within its bounds would be benefited. Economically, therefore, this last plan of reform is the better of the two.

Incidentally to carrying this last scheme into effect, the existing seven tenths of 1 per cent tax on deposits of savings banks (in fact an indirect tax on mortgages) should be repealed, or otherwise the banks would be seriously handicapped in competing with private capitalists in making loans upon mortgage in this State. But if the taxation of mortgages *pro forma* is retained, collection being made at the source for the benefit of the towns where the mortgaged property is situated (as under the division-of-equity plan), then it seems to me that the uniform rate of 1 per cent for the whole State should apply, directly or indirectly, to the Vermont mortgages held by the banks and trust companies as well as to those held by other people.

The existing system, and the two possible reform systems, are now set forth in as clear a form of statement as I can command. In this case it is not that "you pays your money and you takes your choice," but you take your choice and then pay your money accordingly.

GOVERNOR GUILD: The meeting is now open for discussion.

DR. WEST (Washington, D.C.): I would like to ask a question. In what Professor Taylor said about speculation, he spoke of that in one so brief sentence that he almost seemed to confuse speculation in land with speculation in money or credits, which may serve a useful purpose in regulating value. I should like very much to hear Professor Taylor say whether, in his opinion, speculation in land has ever served any useful purpose.

PROFESSOR TAYLOR (Nebraska): Why, it would seem to me that the opening of land in a new country has been a very useful thing, and it has been carried on as a private enterprise. In our town, land speculators have been in the habit of opening additions to the town. They buy twenty-five or thirty acres of land, cut it up into town lots and sell them off at auction, making a good big profit out of them. If this had not been done, the persons who bought those lots could not have acquired them; the land was not for sale by lots; it was enterprise, the enterprise of the parties who put it on the market, that made the land available. In those additions, they put in improvements, sewers, sidewalks, and roadways connecting it with the city. That is a speculation, just like any other, but I do not see why it is not just as legitimate as any other form of speculation.

DR. WEST (Washington, D.C.): I think the gentleman in his answer has mentioned the one useful feature and the purpose which is served by real estate speculation, if that is properly included in the definition of real estate speculation, as I suppose it is; I think, perhaps, what we commonly mean by speculation is something rather different from that, and it seems to me that the real function which the real estate man serves is in advertising the lots and in influencing people to move out into the suburbs. Of course, he does make it easy to obtain small quantities of land, and to that extent, I am willing to admit, he does serve a useful purpose.

GOVERNOR GUILD: Might we not also include in speculation in land a case where private enterprise took flats covered by the tide, filled those flats in and made them available and valuable?

Private enterprise bought those flats on speculation, filled them in, sold them, and thus added taxable real estate to the town, in addition to making the flats available for a useful purpose.

MR. THOMAS (Utah): The Western States have large areas of tillable land that cannot be made available unless water is brought upon it; it must be irrigated. Irrigating companies are formed for speculative purposes; they have their engineers go out and survey for irrigating ditches, as large as may be necessary to bring water upon these lands; they build large dams to hold the water, and then having done all that and brought the water out upon the land, under the Carey Act, which was passed a few years ago, they dispose of this land at a profit. Thus the West has been settled in the last four or five years as never before. Land speculation in that direction has been of great advantage to the Western States; it is going to solve the problem of how to bring in this land, heretofore called desert land, make it habitable and available for useful purposes.

MR. JORDAN (Columbus, Ohio): Regarding this subject, I might say that the ordinary acceptance of the term "land speculation," is where land is held out of sale for the purpose of securing added value — higher prices. The purpose of land speculation is usually exactly the reverse of where land is being brought into use. In case of speculation where land is held out of use, it cannot but be condemned.

MR. PLEYDELL (New York): I would like to say, in view of what the last speaker has said, that those various improvements specified, in the way of irrigation, filling in, etc., could, under any sound system of taxation, be justly separated into improvements, as apart from the site value of the land; thus such an enterprise would not enter into the same classification as the other case of mere speculation.

DR. WEST (Washington, D.C.): The last two speakers have made a very proper distinction, just as the miller in his own mind distinguishes very clearly between the value which he adds to the wheat in the course of manufacture, and the speculative value, which he does not consider at all. So we must distinguish between the value added to land by improvements, and the speculative value of land.

GOVERNOR GUILD: The Chair would like to say a word or two: I understood one of the speakers of this evening in a very admirable address, speaking of how land may be stripped of value in the handling of certain crops upon it, to adduce as an illustration the declining value of New England farms.

A DELEGATE: I meant to say simply that I happened to go through New England this last September. I said to a very aged man that I met there: "How about the old farm? What did you do about it?" "Oh," he said, "I cut the grass off for ten or fifteen years; they don't get much now." I said, "How much do you make — how much do you get out of it?" "Oh," he said, "I get as much out of it that way as I could if I had sold it." "What condition is it in now?" I asked him. "Pasture," he said, "pasture, grown up."

GOVERNOR GUILD: At the risk of having to rule myself out of order for dragging in something that has nothing to do with the case, I beg to refer the gentleman to a report of the Massachusetts State Board of Agriculture for any of the last fifteen years. By that report it is shown that the value of the agricultural product is steadily increasing, because on the whole we are changing our agricultural products. We no longer raise the same crops, the grains, that our grandfathers used to, but we do raise small fruits and garden products, and it is a fact that the Massachusetts cucumbers will bring far more on the land than an acre of wheat or rye or oats. We are increasing the value of our agricultural products every year. Fifteen years ago there was a state department for the disposition of abandoned farms; ten years ago that department was absolutely abolished, and it is a fact that at the last taking of the census from the counties, Middlesex and Worcester respectively ranked thirteenth and fifteenth in the value of their products, as compared with all others of the United States of America. Excuse a little Massachusetts boasting.

MR. FILLEBROWN (Massachusetts): It is said we should agree with our adversary quickly, while we are in the way with him, and I would like to take this opportunity to say that of almost every word uttered by Professor Davenport I most heartily approve; but I wish to take this occasion to correct one error, and I am sure he will thoroughly agree with me in that correction. The

impression prevails that the farm values, which wear out, would be taxed under the single tax. The single tax is a tax upon the site value, not upon any part of that land which requires renewal—not upon any improvement or anything that the farmer has upon his land.

GOVERNOR GUILD: If I may be pardoned one more word in connection with something that came up this afternoon. The gentleman from Washington was good enough to say this afternoon that he thought personal, practical experience should be given, rather than theory, wherever it afforded any light. In the discussion of the value of growing crops and as to whether growing crops should or should not be taxed, several gentlemen have pretty generally stated that they should not be taxed and that they were simply part of the value of the land. I wish to make no argument, but simply wish to assert an experience which I had myself. In 1899, for lack of one better, I was made inspector general of the province of Havana, and part of my duty was to go out and inspect lands adapted to farming. Now, it makes a very great difference whether you regard the crops from the viewpoint of the farmer paying the government, or of the government paying the farmer. Whatever may be the case where the farmer has to pay the government, I invariably found that where the government had to pay the farmer, growing crops were decidedly and always regarded as of taxable value.

MR. ROCKWELL (Washington): My colleague and I have come a long way from home, at the request of the Governor of the State of Washington, to listen to discussions here of different systems of taxation, hoping that we would hear some system discussed or outlined, some plan advanced, that would be better than any system we have in Washington, or that we know anything about. I have sat very patiently and listened with a great deal of interest to the different discussions and the addresses and papers and I have been much impressed.

Now, I do want to say, before taking my seat, that we come here to do something of practical effect in taxation, as well as to hear theories. I am glad to hear the discussions here and the addresses and papers read by theorists, but it is up to people who are in the position of my colleague and myself, as tax commissioners, to put those theories into practice. All of these

theories have been well discussed, well thought out by men who are learned in their business, generally by professors and economists from the different universities and colleges of the country. We are glad to hear those theories, but we do hope at some stage of the game — if I may express it in that way — to hear from some person who has tried some of these theories, and who can tell us the effect in his community.

A DELEGATE: You will not hear it.

MR. ROCKWELL (Washington): So far as the last paper which was read is concerned, we are all more or less familiar with that idea, that is, the taxation of moneys and credits. The last legislature of the State of Washington, in its wisdom — or its ignorance, as you please — exempted or attempted to exempt from taxation all money and credits. For myself, and I think I can speak for Mr. Frost, we think they cannot do it — that they passed an unconstitutional bill. They anticipated themselves by at least two years, because the constitutional amendment which would allow that exemption will not and cannot be put into effect until the people have voted on it two years from now. However, the legislature passed the bill and the Tax Commission has complied with it and has not attempted this year to assess money and credits. It may be that, as my colleague suggests, we shall have a great deal of trouble over it; but some of us took the position that it was not the province of the Tax Commission to construe the law, but simply to enforce the law as found on the statute books. What effect the exemption of money and credits is going to have in the State of Washington, from a practical standpoint, I think we are not in a position to say at this time. I was not in favor of the absolute exemption of money and credits; I was more in favor then and am now of the system that has been inaugurated in Minnesota and New York; but I do say that rather than apply the principle of the general property tax to mortgages and other credits, I very much prefer their entire exemption. I think that all that was said by the distinguished gentleman from Iowa, where he spoke of the absolute impossibility of making people return this class of property for taxation, is absolutely true — that is, he says it is true, and I am willing to swear it is true in Washington — I don't know, of course, about any other States. It is

absolutely senseless and nonsensical to think that if a man has a mortgage in the State of Washington drawing 7 or 8 per cent, he is going to return that mortgage for taxation where he will have to pay 3 or 4 per cent of that amount for taxation. He will not do it, and he would be insane if he did. I think that the recording tax is a very good system and probably is the solution of this problem to a great extent. Matters and things of this kind are the subjects we would like to hear discussed. Questions of this practical nature we are very much interested in, and I hope there will be full and free discussion from practical people, dealing with the practical subjects, such as the address of the gentleman from Iowa.

PROFESSOR ADAMS (Wisconsin): In the county of Clayton, Iowa, there have been placed on the assessment sheets in the last six or seven years, \$3,000,000 dollars of mortgages, and the rate of interest is about 5.25 per cent, as I remember it. If one wants tangible facts about the successful collection of taxes on mortgages, I recommend to the consideration of such person Clayton County, Iowa.

A DELEGATE: What is the tax?

PROFESSOR ADAMS (Wisconsin): The tax is about 1 per cent.

PROFESSOR TAYLOR (Nebraska): When I said that interest and credits were proper subjects of taxation, I meant it to be understood that I did not expect that notes, bills and private loans by private money lenders and the note shaver were always to be gotten at, but I meant that the fact that those were proper subjects of taxation, would naturally guide practical men in laying taxes so as to strike that class of men who should be taxed on their credits, but cannot be reached through their credits, in some way that would be proportionate — and that is the French system. The French, by a system of stamped paper and stamps put quite a little tax on private loans, the loan or the commercial paper not being good unless it bears that stamp upon it. They have a business tax also, and as you probably know, business taxes are growing very rapidly throughout this country. The French system of business taxes is extremely complicated; it is a taxation system in itself.

MR. ROBINSON (Kentucky): I believe there is hardly a man on this floor who is not surprised at the confession and the

admission as to the inoperation and the non-enforcement of taxation upon intangible personal property in all of our States. Now, it seems to me we are coming down to something that is practical, and if this Conference does nothing further than to enable us all to go home and try to have that one feature corrected, either by striking out taxation on much of this intangible, elusive personal property upon which the State needs no revenue at best, or by devising some remedy — I believe this Conference will have accomplished a great work. I recall the close of a sentence in one of the chapters in a book by David A. Wells, who I suppose all of us agree was one of the greatest economists of his time, where he makes this statement, that any attempt to tax intangible personal property is more productive of injury than of revenue. I think we have had abundant testimony to that fact in this experience meeting. The State of Pennsylvania, as you no doubt know, has a very moderate rate on personalty, forty cents, I think, and that State realizes \$6,000,000 per annum revenue from that class of property, because the rate is made reasonable. In our State, in the city of Louisville, we have just voted an issue of four millions of bonds to build sewers; the courts decided that the city of Louisville could not tax those bonds in the hands of her own citizens, but strange to say, the Circuit Court say that the State of Kentucky and the county of Jefferson must tax them. The State of Kentucky and the county of Jefferson get a direct benefit from this public improvement, and yet they tax those bonds so as to reduce the income of citizens of Kentucky holding them to a three and one fifth rate of interest, and the result is, we cannot sell the bonds.

A DELEGATE (Iowa): Just a word in regard to Clayton County: The fact that these mortgages have been taxed in Clayton County is one of the best arguments against trying to tax them, for the reason that every mortgage that is taxed in that county is owned by a resident, usually by the widows, or the estates. The banker or other business man who has mortgages on record in that county and is a resident there, can offset his mortgage by his indebtedness — by a mortgage on land in Minnesota, for instance. The man who lives over in Wisconsin comes to Clayton County and makes a loan, and he has far the best of it, because he does not pay any tax. The man in Clayton County who

wishes to loan his money in that county must pay a 2 per cent tax, while the Wisconsin man pays none. That is certainly unjust.

MR. CORAY (Utah): Just a word or two. There is, perhaps, no doubt that such a tax can be collected, if it is small, but it is a question of public policy whether you want to add another tax to the burden of the man borrowing the money. That is where the tax would be collected. The man loaning the money would not pay the tax, but it would be added to the tax of the man who borrowed the money.

PROFESSOR ADAMS (Wisconsin): I do not want my remarks to be misconstrued. It happens to be a fact that a large part of that Pennsylvania tax, personal tax, is raised by mortgage.

A DELEGATE (Washington): This question of money and credits is one in which the people of Washington are more vitally interested than any other. There are some features in connection with the taxation of mortgages and other credits that do not seem to have been considered by the gentlemen who have talked upon this subject. It occurs to me that the first proposition in considering a system of taxation is to ascertain the distribution of the burden of taxation, expressed by the taxation of the particular class of property. I have made some exhaustive personal investigations of the conditions existing in our own State. We find all of the evils complained of under the general property-tax system. For instance, in the county of Thurston, with banks having in the neighborhood of five millions on deposit, three years ago all the money returned for taxation was the sum of \$2000, and that was a life insurance policy received by a widow — that was the whole of that return in the county. Now, these are the conditions we find: that the class of property most heavily taxed, the class of property that is assessed at a higher proportion of its actual value than any other property, is the ordinary home of the ordinary man; the home that cost him from \$1500 to \$4000. Following that class, we have farms, agriculture and live stock; following that, we have farm lands. We find that manufacturing property, shipping property — we have a great deal of shipping out there — business property in the cities comes in with a very much smaller proportion than the other classes. Upon making investigations

in other counties, among them, King, the largest and most populous, I found that more than seven tenths of all the money borrowed and secured of record is borrowed upon the class of property that is escaping the just proportion of the burden of taxation levied upon real property; it is borrowed upon the manufacturing concerns, upon the immense business blocks, and upon the class of property that is assessed very much lower than the class I have mentioned. I think it is true that we must go, not into theories, but into actualities. The man who borrows money in small amounts, the man who borrows upon his home, is not governed in the amount of interest that is charged to him by the current rate or the market rate, but he must pay just all that he can pay. He does not go out into the market and seek to borrow money, but he is compelled to borrow from his neighbor, and he pays just all that he can pay for it. Money exacts all that it can get from that class of borrowers. On the other hand, the large loans, made upon a large enterprise, are made at a very much lower rate of interest. For instance, I think the average rate is about $4\frac{1}{2}$ per cent; the rate of interest on the home borrower is nearly, almost always, 8 per cent. The money tax upon money and credits does this. It does not affect the rate of interest paid, perhaps, by the large borrower, but it may compel the small borrower to pay more. If I have offered some food for reflection, I shall be very well satisfied.

MR. WALLACE (Minnesota): The burden is being shifted in our State to the borrower of large loans that are being made there. I was one of the authors of this measure and had as much as any one to do with it. We did it with our eyes open, believing that we could use it as an object lesson in bringing the matter more forcibly before the people of our State. The fact is that the borrower pays the tax,—and there is no question and cannot be any question about it,—and we believe that we have given the people of Minnesota enough of an object lesson so that at the next session of the legislature we shall wipe out all taxes on mortgages.

SIXTH SESSION

THURSDAY MORNING, NOVEMBER 14, 1907, 9:30 TO 12:30 O'CLOCK

CHAIRMAN, HON. A. C. RUTHERFORD, PREMIER
OF ALBERTA, CANADA

PROGRAM

1. TAXATION OF CITY REAL ESTATE AND IMPROVEMENTS ON
REAL ESTATE AS ILLUSTRATED IN NEW YORK CITY.
Professor John H. MacCracken, Ph.D., New York Uni-
versity, New York, N.Y.
2. THE TAXATION OF REAL ESTATE AND REAL ESTATE IM-
PROVEMENTS.
F. A. Derthick, Chairman Committee on Taxation, Na-
tional Grange, Master Ohio State Grange, Mantua,
Ohio.
3. MUNICIPAL TAXATION OF INTANGIBLE WEALTH.
Professor Jacob H. Hollander, Johns Hopkins University,
Baltimore, Md.
4. REFORM IN MUNICIPAL TAXATION.
Professor Charles Edward Merriam, Department of Politi-
cal Science, University of Chicago, Chicago, Ill.
5. INCIDENCE OF TAXATION.
A. C. Pleydell, Secretary of New York Tax Reform As-
sociation, New York, N.Y.
6. THE BASIS OF ASSESSMENT IN TAXATION.
Dean F. W. Blackmar, Graduate School, University of
Kansas, Lawrence, Kan.
7. BUSINESS AND PROFESSIONAL TAXES AS SOURCES OF
REVENUE.
Professor Harry Alvin Millis, Department of Economics,
Leland Stanford Junior University, Stanford University,
Cal.
8. DISCUSSION.

TAXATION OF CITY REAL ESTATE AND IMPROVEMENTS ON REAL ESTATE AS ILLUSTRATED IN NEW YORK CITY

BY PROFESSOR JOHN H. MACCRACKEN, PH.D.

New York University, New York, N.Y.

"To most people," says William Smart,¹ "taxation is a great mystery. To a few it is the most fascinating of subjects. There seems to be no middle course; either a man has thought so much about it that his utterances are unintelligible to the people, or he cannot discuss it intelligently because he does not know its alphabet." It is the object of this Conference, I take it, to mediate between these extremes.

The topic assigned to me, while perhaps as far reaching as any in its importance, is not one of the tax questions about which the conflict is now raging in America. Nor do I introduce a discussion of it at this time with the idea that reform should begin at this point. My object, rather, is to show the merits of the present system of land taxation in New York City, and thereby increase the dissatisfaction with less desirable forms of taxation, and to stimulate the search for substitutes therefor. The present form of the tax on improvements, I shall try to show, is less admirable in its working than the tax on land, and I shall suggest a different method of levying and collecting this tax. But to avoid misunderstanding, I wish to say at the beginning that whatever the faults of our tax system, as we have it in New York City, and we will all admit that they are serious and glaring, the tax on real estate is worthy only of admiration, and is probably on the whole, the most equitable in its distribution, the simplest in its administration, and the most productive in proportion to the conscious sacrifice involved, and carries with it fewer evil consequences than any tax system hitherto devised. To secure an annual revenue

¹ William Smart, "Taxation of Land Values and the Single Tax," p. 32.

of \$80,000,000 at an expense of about \$600,000 for assessment and collection, with no greater sacrifice than is involved in the payment of a rate of $1\frac{1}{2}$ per cent on a 70 per cent valuation, is a fine illustration of Colbert's supreme art of taxation—the plucking of the greatest number of feathers with the least amount of squalling. Other criteria of good taxation it meets as well.

Technically, taxes on franchises and taxes on the real estate of corporations are included under taxation of real estate. For the purposes of the present paper, however, I wish to exclude these forms of real estate taxation and treat only of taxation of lands and buildings, or real estate in the common usage of that term.

There are certain general principles which I must take for granted as the limits of this paper will not permit their discussion except incidentally. The first of these is that enunciated as the first plank of the platform of The National Tax Association; viz., "The attempt to tax all classes of property in the same way and at the same rate produces gross injustice." There is no more elusive concept in philosophy than the concept of justice. The simplest notion of it is the same penalty for the same offense, or the same reward for the same good deed, to give to every man his penny, or take a penny equally from every pound. And as soon as we leave this sort of crude justice and begin to take circumstances into account, and to beat with few or many stripes, as the case may warrant, we become involved in this psychological and sociological age in all sorts of difficulties. Yet just as our school system is suffering to-day because of the notion that the State in order to be just must give the same sort of education to all its children, no matter how different the needs or aptitudes of the children, so our tax system, while outwardly and formally professing to attain justice and equality, treating all property alike, is in its actual working and effect unjust and unequal. The general property tax reflects the ideals of the individualism of a past generation, when every man was accounted a full man, substantially as able to take care of himself and bear his share of the burden as any other man — when it was supposed that with a fair field and no favor, rewards would be equal to merit. It was a suitable tax for a day when, as in the case of the inventory of my great-great-grandfather's estate, the original of which I saw this

summer in the old county records, it was expected that each pair of linen and buckskin, as well as of velvet breeches, should all be itemized in the total of the estate.

Starting in pursuit of the ideal of equal justice, we have been blind to the expense and evil consequences incurred in the effort to see that no wealth should escape its fair share of taxation. But equality of treatment is not the loftiest ideal. It must always be subordinate to the highest general welfare. We must recognize that equality of treatment, while one of the ideals all modern government seeks to reach, may be secured at too high a price. With the growth of large cities, the division of labor, the specialization of function, the complexity of the relations of the city dweller, and the mutual interdependence of city people, we are coming to look at things from the standpoint of family or community interests, rather than from the standpoint of the individual, and in discussing the relative merits of various systems for producing revenue, lay less stress on securing an equal contribution from all wealth and more stress on securing a system which will yield the community the greatest amount of net revenue with the least individual hardship or injustice, and the least detriment to the interests of the whole community. It is a mighty work, however, that this convention has set itself, of trying to so broaden the view of the individual citizen on the subject of taxation that he will concede that it is for the general welfare for him to pay 1 per cent on his thousand dollars worth of property because of the nature of the property, while his neighbor pays nothing, at least directly, on his thousand dollars of value. What has been accomplished in the State of New York in the matter of the taxation of mortgages is, however, good evidence that such campaigns of education eventually succeed, and that it is possible to overcome the American prejudice and to treat different forms of property differently.

The second principle which I must ask you to concede, is that city land and country land are two different things so far as taxation and their economic uses are concerned, and that, therefore, a State is justified in adopting a different system of taxation for real estate and real estate improvements in large cities from that applied to farm lands. There is less

difficulty in getting New Yorkers to concede this than citizens of other States, because we have finally succeeded in providing the State with revenue without the use of direct taxes for that purpose, so that it becomes a matter of county concern only as to how our land tax is administered. I fear, however, that even in this convention if I were to undertake to convince some of you that city land and farm land were different things to all practical intents and purposes, I should be reminded that this is a distinction which our classical economists have thought they could safely ignore. I do not propose to discuss the theoretical question as it would lead us too far afield, but to assume, with your permission, the truth of it as a hypothesis.

Frankly, it seems to me futile to discuss improved systems of land taxation, if we are to have one and the same law for farms and city lots. Were we to proceed with that object in view, we should probably not come to any more satisfactory conclusion than the gentlemen discussing the two sides of the shield.

And thirdly, I must ask the most questionable of the three concessions; namely, that it is justifiable to utilize the taxing power as an agent for attaining social ideals, as well as for revenue.

It is a common practice to deny the last on theoretical grounds, and then make forbidden use of it on practical grounds. We do so use the taxing power in our tariff system to develop a varied and complete civilization. In New York and other States we use a high license tax to diminish the consumption of intoxicants. Many localities are trying to tax signboards into beauty and respectability. I shall ask you, therefore, to concede, for the purposes of this paper at least, the theoretical right of a community so to adjust its tax on land and land improvements as to promote ideal conditions in land distribution and in improvements, provided it avoids injustice and finds it advantageous so to do.

May I take it for granted also that we all recognize three evils growing out of our present land system in large cities, which may be stated as follows:

1. The taxation of improvements is a factor in rental values and is not distributed according to the ability to pay taxes. It bears with undue heaviness upon the poor.
2. The improvement tax, while a direct tax on property,

becomes, psychologically, an indirect tax for the rent payers, who in a city like New York constitute more than three fourths of the population and hold the political power.

3. The diversion of the whole increment of value of land into private pockets constitutes a perpetual tax on succeeding generations.

I think we can safely admit these evils from the standpoint of the city family without committing ourselves to any one remedy.

Taking up now the actual working of the present law in New York, we find that the city budget required the present year in round numbers, \$130,000,000, of which amount about \$102,000,000 must be raised by taxes, \$29,000,000 being the estimated revenue of the general fund. The revenues of the general fund include a great variety of items, the most important being the receipts from the excise tax and receipts from the sale of bonds, and the repayment of the cost of street and park openings with interest. In 1906 the receipts from taxes were approximately \$80,000,000 from taxes on real estate exclusive of franchises and real estate of corporations; \$1,500,000 from taxes on franchises and real estate of corporations, and \$4,500,000 from taxes on personal property. Of the \$80,000,000 derived from taxes on real estate, again approximately \$50,000,000 is derived from a tax on the land and \$30,000,000 from a tax on improvements on the land. The total value of New York real estate is \$5,700,000,000, of which amount 62.5 per cent is land value and 37.5 per cent is improvement value; \$1,150,000,000 of real estate value in addition is exempt. Brooklyn is the only one of the five boroughs in which the buildings are rated as more valuable than the land, the per cent of improvement value being 54.7 as compared with 32.8 of Manhattan. This in spite of the fact that the skyscrapers and palaces are in Manhattan. Statistics collected by the Hon. Lawson Purdy of the New York Tax Department show that the relative value of improvements and land is very much the same in Boston as in New York, but that in other cities, in which statistics are available, the value of the improvements tends to equal or exceed the land value. Thus, in Baltimore, the value of the buildings is 56 per cent of the total value. If the land and buildings of New York City

were divided equally among the population, each man, woman, and child would be entitled to a lot worth \$828 and a house worth \$500, while in Boston his lot would be worth \$1067 and his house worth \$692, and in Baltimore, his lot worth \$232 and his house worth \$296. It is seen, therefore, that we are dealing with the wealth and revenue of an empire. As the Department of Taxes pointed out in their last report, the assessed value of the land alone, exclusive of improvements, is greater than the value of all the real estate improvements included in the State of Pennsylvania, while the annual increment of New York real estate value is almost as great as the entire value of real estate in St. Louis.

The method of assessing real estate and improvements on real estate in New York City is as follows:

There are 463,000 different parcels. The work is divided among a certain number of deputy tax commissioners in each borough. These deputy tax commissioners are, for the most part, residents of the boroughs in which they act, and are attached to the branch offices of their respective boroughs. They begin work on the first Tuesday of September, using accurate maps, which have been prepared for them, on the scale of fifty feet to the inch, giving all the necessary dimensions. They are allowed somewhat less than four months for the work and the annual record of the assessed valuation of the real estate is completed and open for public inspection the second Monday in January. Taxpayers are allowed until April 1 to present grievances, and corrections are made by the board of tax commissioners during April and May. Assessment rolls are transmitted to the board of aldermen the first Monday in July and the tax rate is fixed in August. The taxes become a lien upon the first Monday of October, and are payable by the first day of December. Taxes for the current year paid before June 1 are received by the receiver of taxes. Taxes paid subsequent to that time are paid to the Bureau for the Collection of Assessments and Arrears.

The adoption of the block system for the records of the register's office has given the tax department also the benefit of a most satisfactory system of maps for the greater part of the city. There are still portions of the Bronx and Brooklyn,

as well as the boroughs of Queens and Richmond, where the block system has not yet been completed and they are still divided according to the old ward system. In addition to these map books, each deputy is provided with field books which give, in addition to the usual assessment record, the assessed valuation of each lot for seven years; recent sales with the consideration, if known; mortgages on the respective properties with the names of the institutions lending the money, if the institution is one limited by law to loans not in excess of a certain percentage of the market value; recorded leases with the period and rental, and any other data which may be indicative of value.

Since 1903, the value of the real estate unimproved and the value of the real estate with improvements have both been reported.

The value of the real estate is reached by first adopting a unit of front foot value; that is, the value of a lot 100 feet deep with a frontage of one foot on the street. When lots are irregular, the value is determined by the Neill or Hoffman rule. When a number of lots can be utilized to better advantage under single ownership than as respective lots, an addition may be made to the unit of value for plottage. By the use of units of value comparisons of valuation in the same neighborhood are greatly facilitated.

The maximum value of improvements is reckoned on the basis of the cost of replacement. To determine the cost of replacement, the number of square feet of floor surface is determined by multiplying the size of the house by the number of stories; air shafts and irregularities being disregarded. The number of square feet is then multiplied by certain factors in general use for the different classes of buildings, as follows:

Modern office buildings	\$4.00 to	\$8.00
Modern hotels	3.50 to	8.00
Elevator apartments	3.00 to	5.50
Flats	2.00 to	3.00
Ordinary stone or brick dwellings	3.00 to	5.00
Very costly dwellings	up to	10.00
Frame dwellings	1.00 to	3.00
Lofts	1.50 to	3.00
Factories	1.00 to	3.00

Deductions are then made, taking into consideration first the suitability of the buildings for the site, and second, its depreciation from age and wear and tear. It is evident that the separation of the value of a given property into land value and improvement value must, in many cases, be an arbitrary one. In desirable business or residence sections, the highest land value would attach to the vacant lot. Under prevailing conditions, therefore, when the land is wanted almost entirely for new improvements, the value of the old improvements to the purchaser is only its value as wreckage or possibly the improvements are a detriment and diminish the value when time becomes an important factor. As a result of this fact, the assessed improvement value, as compared with the assessed land value is much lower than we should expect. Professor Seligman in his book on "Incidence of Taxation" remarks incidentally, "that the building tax tends to form the greater part of the total tax. The average dwelling house in New York City," he says, "for example, is worth when first built from two to three times as much as the lot. In tenement house districts, the proportion is slightly, if at all, less, except in the case of the tumble down wooden houses which are fast disappearing." Such was the opinion of so well informed a judge of tax values as Professor Seligman, prior to the separation of the two valuations on the tax rolls. As a matter of fact, the last report of the tax commissioners shows that in every section of Manhattan and the Bronx the improvement value is less than the land value, the percentage ranging from 53 per cent to 83.9 per cent, the average for the two boroughs being 61.8. Brooklyn is the only borough in which the improvements are assessed as of greater value than the land, the average percentage of land value for the whole borough being 44.8 per cent, and ranging in different sections from 35.7 per cent to 71.1 per cent.

A study of the assessment roll of the various blocks in the city indicates that especially in the case of older buildings, the valuation of the improvement falls much further short of the cost value, or replacement value, than the valuation of land falls of the market price. Thus, for example, a row of millionaires' residences on a fashionable street are valued at

\$12,000 to \$15,000 each although they stand on land valued at \$90,000 to \$105,000, and although the houses are recognized as suitable improvements for the site, though not of recent construction. On another fashionable street the improvement valuations run from \$25,000 to \$35,000, the houses standing on land valued at \$120,000 to \$150,000. It is to be noted, however, that in the same street a modern house recently erected, to replace one of the older houses, is valued as high as \$90,000. In the newer uptown district, a \$50,000 house on a \$55,000 lot is not an uncommon type, although we find there are many cases of houses built before the division of the assessments on the tax records, of \$10,000 or \$15,000 houses on \$55,000 or \$60,000 lots. There are quite a few cases of \$80,000 houses on \$65,000 lots, but a proportion of this sort is found, as a general thing, only in the case of a house built within the last two or three years on a lot which is still in the outskirts of the fashionable neighborhood. If, on the other hand, we consider the relative assessments in the business section, we find, for example, that in the case of the Park Row Building, which was the highest building in the city up to the present year, consisting of twenty-five stories and a tower, of the total valuation of \$3,370,000, \$1,365,000 is set down as land value and \$2,005,000 as improvement value. This is one of the notable instances where it has been found possible and desirable to place an improvement on downtown New York land of greater value than the land.

The improvement forms a striking contrast to the improvements on the land immediately adjoining. On these lots stand old-fashioned five-story buildings and the total valuation of the three lots, \$775,000, is divided into \$690,800 as the value of the land and \$84,200 as the value of the improvements, the improvements, therefore, being but a little over one eighth the value of the land. Taking the Manhattan Life Insurance Company Building, a modern eighteen-story building, 66 Broadway, it appears that of the total valuation of \$4,050,000, \$2,760,000 is credited to the land and \$1,290,000 to the building, so that a modern office building on this location, although eighteen stories high, is valued at less than one half the value of the land. The typical brown stone house of the most fashionable New York residence section, costing to build \$30,000 to \$50,000,

is valued according to its width and height from \$5000 to \$15,000. Residences for which the owners refused as high as \$400,000, including land and house, and which are still occupied by the owners as residences, are valued as low as \$10,000 in the Fifth Avenue section where business has begun to encroach on the residence area. It can be seen from these instances taken at random that the assessed improvement value has comparatively little relation to the cost of the original improvement or the cost of replacement, and it may be stated as a general principle, that the value added to property in any good locality by desirable improvements is eventually absorbed by the land value, the value of the improvement tending to diminish as the land value increases. The extent to which this is true in a rapidly growing city like New York shows that in discussing the taxation of land and improvement values, or the taxation of rental values in such a city, we are dealing with quite a different problem from that with which we should be dealing, for illustration, here in Columbus.

In order to equalize taxation in Brooklyn and the outlying boroughs, which in 1898 were consolidated with the old city of New York, with taxation in Manhattan, the assessed value in Brooklyn being considerably higher in proportion to the market value than in Manhattan, it was determined in 1903 to assess all real estate at its full market value. Other considerations, of course, entered into the change; namely, the desirability of increasing the borrowing capacity of the city, which is limited by law to a certain percentage of the assessed valuation, and the opportunity for political capital which could be made out of a nominal reduction of the tax rate from 2.27 to 1.41. As a matter of fact, this new method of valuation worked little hardship except in the case of some of the great commercial buildings in process of erection at the time, the cost value of which was readily ascertainable and which came in for a much higher assessment than would have been made under the old system. The growth of the city of New York and the great increase in realty values since that time have been such that, in spite of the rapid marking up of values at that time, the assessed valuation to-day, taking the city as a whole, does probably not exceed 70 per cent of the

market value, and in many cases is not over 60 per cent. An examination of the books for different parts of the city and for all classes of improvements, whether business houses, private dwellings, or tenement houses, leads me to believe that the assessed valuations of land lag about 30 per cent behind the extraordinary rise in values which has occurred the last three years. In the case of unimproved property in many cases, the assessment is about 55 per cent to 60 per cent of the market value. In New York among the potent factors in keeping assessments below the actual market value is the strong community feeling in the different boroughs and the rivalry which exists between them. It is a condition very similar to that which exists among all the cities or counties of any State, and which gives rise to the necessity of a state board of equalization. Thus, in New York the Comptroller, the chief financial officer of the city, a Brooklyn man, is disposed to criticise the assessments in the Bronx as too low, while the people in the Bronx admit that their valuations fall below market value, but are not willing to increase them so long as Brooklyn assessments are kept so low. At the present time, the question is being discussed by the charter revision commission of New York as to whether the city at large gains or loses more on the whole by the fostering of this local interest and local pride. In the matter of the assessment of land, at any rate, it would seem desirable to provide occasionally for an interchange of assessors. It is impossible, of course, for one man to be thoroughly familiar with values in more than a comparatively small section. It might, however, be illuminative to him to spend certain days in each year in company with the assessor of another borough, making the rounds with the latter in his duty of assessment.

How successfully the work of assessment is done and how generally acceptable the work of the department is to the great mass of taxpayers, is shown by the fact that the total of 463,000 assessments occasioned only 3650 applications for reduction. Whereas, in the case of the personalty tax, more than one half of the names assessed are stricken out before the levying of the tax and only about half of the remainder is collectible. If, therefore, we proceed to a consideration of the weak spots of real estate taxation, it will not be because of any widespread

popular demand for reform in this direction, on the part of the taxpayer, but rather for the sake of indicating certain general considerations which should not be lost sight of in any steps which may be taken toward improvement in the general system.

First, therefore, it seems desirable that the New York law, requiring the assessments of land at the sum for which it will sell under ordinary circumstances, should be strictly enforced. A study of assessments in both city and country indicates that the percentage of value at which property is assessed represents the point at which the opposing interests reach equilibrium. It is evident that to assess property at, say, two thirds of its value makes the administration of the law much simpler and diminishes discontent. Thus, it is the common practice in New York, when a taxpayer who feels that he is being taxed too high compared with his neighbor goes to enter a complaint, for the clerk to meet him with the question, Would you sell the property for the assessed value? and in a large proportion of cases the complaint is checked before it has become fairly articulate. Were the assessed value and the market value close together, the bluff of the tax office could not be used to such good advantage. Of course, it is no true answer to the complainant under the present system to reply that he should be content so long as he is taxed on less than market value, because the justice of any tax lies not so much in its amount, as in its equal distribution. Assessments at market value, therefore, cause much closer examination of the work of the assessors and conduce to justice as between different taxpayers, though they may increase the difficulties and cost of administering the law. In New York, just at present, assessment at full market value is desirable to permit bond issues for subways, but as this argument for full assessed value is counterbalanced by the argument that it conduces to municipal extravagance, I do not urge it.

As the second weak point in our present system, I would mention the relatively lower assessments placed on acreage property than on single lots. Of course it is difficult for the assessor to determine how far farm lands have increased in value until they are sold or subdivided. There has been too much readiness in the past, however, to regard the holder of

large estates as one who is kindly serving the community by carrying land for it until the community should be able to use it, and therefore as worthy of special consideration. Thus, the attitude of the city toward the Astor estate, the largest investor in New York land, tends to be that of the officials of a corporation to its chief stockholders, who are always ready to back the concern by purchases of any of its stock which may be thrown on the market. The city of New York is undoubtedly indebted to the Astor estate for the many fine improvements erected on their land; but the debt is several fold canceled when the estate, as in the case of the annexed district of the Bronx, buys up a large section of outlying territory with a settled policy of holding it without improvement for many years, the bill for carrying it unimproved to be finally settled by the community. It is so evidently to the general interest of the community that acreage property in the city limits should be subdivided and improved rather than held for a rise in values, that it would seem that the assessor might well err on the side of assessing acreage at more than it would bring when subdivided, than to fall so far short of this value as has been the practice in past years.

There can be no question that Mr. Henry George touched on one of the most vital problems of the modern city in pointing out the burden laid upon the modern city community by the diversion of the so-called unearned increment of land to private pockets. It is by no means necessary that we should agree with Mr. George in his contention that the individual has no just right to the property represented by the rent value of land, in order to recognize the truth of the statement that the diversion of the increment of land value to private interests constitutes a very serious tax on the succeeding generations and that it is to the interests of the community, as a whole, to minimize this tax whenever it can be done in a way which will not cause more evils than it cures. In Germany, the experiment is being tried of reaching this end by taxing directly the increments of land value, thus taking for the common welfare a certain proportion of the profit. In America, since the evil manifests itself most prominently in the withholding of land, by speculators, in the suburbs from improvement, the remedy most commonly

discussed has been to exempt improvements from taxation and throw the whole burden upon the land, in the hope that this would stimulate improvements and discourage the holding of unimproved land for a long term of years, until the necessities of the city force it to pay a price sufficient to cover the cost of holding it. It would be interesting to see the experiment tried in some city, as it is very doubtful whether it would accomplish the desired results. In New York, for example, the percentage of improvement value to land value is such that if the whole tax were charged against the land, and nothing against improvements, it would only increase the tax rate from 150 to 225, and I am of the opinion that the land could carry the higher rate, even without improvement. There could be no question that such a system of taxation would increase the erection of buildings, both for business and for residence, and would reduce rents for a time until general economic laws made themselves felt. It would also presumably depreciate the price of unimproved land and increase the value of improved property until buildings could be erected in sufficient number so as to appreciably increase the supply. It is evident, also, that under such a system of taxation it would be desirable to limit the size and height of buildings that might be erected on a given area, as otherwise too great a stimulus would be given to the erection of skyscrapers to the detriment of the general public and the overloading of the street and sewer system. It goes without saying, also, that to adopt such a system of taxation would be to surrender any thought of dividing the tax burden evenly between different amounts of visible property; thus, for example, in the case of the Park Row Building, already referred to, the owners of the Park Row Building would presumably pay the same tax as the owners of the five-story buildings adjoining, the tax in each case being approximately \$6750 per twenty-five-foot lot, while now the tax is respectively about \$11,000 and \$4000 per twenty-five feet. It is evident, therefore, that any sudden adoption of such a tax would create great havoc in real estate values and would probably conduce to overbuilding, the erection of new office buildings with modern improvements causing tenants to leave the older buildings and diminishing their rental value. Whether the decrease in rental

value would exceed the saving in taxation would depend on so many factors outside of the question of taxation, that it cannot be determined theoretically for any given time or place. The consideration which has made the proposal popular with the people at large has been the assurance that such a form of taxation would reduce the family rent. I think it probable that this result would temporarily follow, and would be in itself a very important consideration for a community in which a large part of its population spends from one fifth to one third of its earnings for the item of rent alone. And if it be true that the tax on land values cannot be shifted to the occupier, it would seem that the renter must eventually gain not only the saving of $1\frac{1}{2}$ per cent on the improvement, but must gain more than the equivalent of that amount by reason of the great stimulus that would be given to the erection of houses in outlying districts, and the consequent increase in the supply, the demand presumably remaining unchanged. It is the last element, of course, which it is difficult to estimate or forecast, it being probable that in many cases the family which had been contenting itself with a \$35 flat would, if the price dropped to \$30, not devote the \$5 a month to other objects, but would spend it to secure a larger flat or better located flat, and the family which had been forced to content itself with three rooms, would demand four rooms, so that the demand, instead of remaining stationary as the supply increased, would doubtless increase with the insatiable hunger and needs of a great city population. As I have already said, I think it would be worth while to have the experiment tried in some one of our smaller cities in the hope that making due allowance for all local conditions and temporary prosperity or depression, we might arrive at some general notion of the outcome of such an experiment when the psychological processes of a city population, as well as the working of abstract economic laws, are taken into consideration. Were the experiment to be tried, however, it is evident that the change should not be made abruptly, but that it should be made by an arbitrary addition each year for ten years, to the tax on land, whether improved or unimproved, of an additional tax at a rate on the assessed value of the land sufficient to yield one tenth of the amount now yielded by the tax on improve-

mènt, the rate of the tax on improvements being correspondingly diminished. Were the experiment tried in New York, the practical working of such a system would be the increase of the tax rate on land the first year from 1.50 to approximately $1.57\frac{1}{2}$, and the decrease of the tax rate on improvements from 1.50 to 1.35, supposing the assessed valuations and the revenue of the city to remain stationary. Such a shifting of the burden of taxation through a period of ten years could, I judge, be accomplished without producing chaos in real estate values, the change being not a greater one than owners of real estate run the risk of in New York in any year, as the result of extravagance by the state legislature or city officials. As I have already indicated, however, the evils such a change threaten to bring with it in such a city as New York, seem to be so great as probably to counterbalance the somewhat problematical good which might be accomplished.

I have, therefore, no solution to offer of the question how the community can retain for itself more of the increment of land value which it creates. The remedies seem all as full of evil as the disease. There is, of course, one complete solution of the difficulty, and that is for all the citizens to follow the example of the professor of economics in Switzerland, who told me that Mr. Henry George's book made such an impression on him, that he at once went out and bought some land in the suburbs of his Swiss city and that he had in this practical way proved to his own satisfaction the reality of the unearned increment. If we should all do likewise, the distribution of increment would so far be promoted.

As a compromise between the present system and the total exemption of improvements from taxation, it has been suggested in New York that the first \$3000 assessed value of improvements be exempt from taxation. The arguments advanced for this system are: first, that it would encourage the erection and ownership of individual residences by families in outlying sections, and would be fruitful in producing the benefits to the community which it is generally acknowledged arise from the ownership of a home. Secondly, that it would make it profitable for the holders of large tracts of unimproved property to improve the property with a class of improvements which

would increase the supply of homes for working people and diminish rents. Thirdly, that by stimulating the ownership of individual homes it would cause a wider distribution in the community of the increment in land values.

The objections to the proposed compromise are readily apparent. However much we may admire the one-family house of the last generation, and however freely we may concede the advantage which it holds for a community in the preservation of family life and the better facilities it offers for the bringing up of families of strong, healthy children, we are wasting our time if we turn our efforts to preserve to this generation the ideals of the last. We may as well recognize that the ideals of the present generation have grown under the force of circumstances in other directions. We cannot suppose that it is without reason that the modern apartment house has supplanted the one-family house to so large an extent. It represents the trend toward specialization which affects all parts of our city life. The average city family, when it has met the demands made upon it by the various work and occupations of its members, has but a small margin of time and money for the thousand and one things which the maintenance of an individual house requires, as compared with an apartment. This is not the place to argue whether the thousands of families who go over into Brooklyn and assume the disadvantages along with the advantages of the individual house get more out of life than the thousands of families who fill the apartment houses of Harlem. The fact remains that the latter number is increasing and the former decreasing, and the tide in favor of the apartment house is too strong to be affected by any reasonable use of taxation. If, therefore, we are to have the exemption of the first \$3000 of assessment value on the theory that a house equal to the means of half our population can be erected for that price, the rapidly increasing number of flat dwellers will at once ask with good reason, why should not our flats be capitalized and exempted in a corresponding amount? Unless the city is prepared to assume the functions of a paternal government and to say to its citizens, "the majority of you who are seeking flat life, while you may be seeking that which promises you the greatest amount of immediate ease and comfort, are not seeking the form

of life which contributes the most greatly to the ultimate welfare of the State," it would not be in a position to exempt the \$3000 house, while it failed to exempt each apartment of the ten-family flat for the same amount. It seems to me, therefore, that any compromise which might be made will necessarily be in the direction of the exemption of a certain percentage of rental value, and in that case, I think the exemption should be for the purpose of discouraging the holding of unimproved land for speculative purposes rather than for the purpose of promoting the erection of homes, and that the exemption should apply equally, therefore, to residential and business property.

This brings me to a consideration of the third and last weak spot which I would point out in our present system, viz. the method of assessing and taxing buildings as distinct from land. It is true that when the city of New York determined to enter upon its tax rolls the value of the land unimproved and the value of the land improved, no provision was made for the taxation of improvements, as such. The tax remains to-day as it was before 1903, a single tax on real estate, and doubtless one of the reasons why this entering wedge of a distinction between taxation of land and taxation of improvements was permitted, was that it was thought, and wisely, that to require a full valuation of land unimproved would necessitate the addition of at least some value for the improvement, and would, therefore, help the assessor to a realization of the full market value, and make the marking up of values which occurred in that year more plausible. Whatever the various motives which led to the adoption of the plan, however, we may all congratulate ourselves that it was adopted, and that we have the exceedingly illuminating statistics which Mr. Purdy has given us in the annual report, to which reference has already been made, as data for the intelligent comprehension of just what contribution is charged against the wealth invested in city improvements, and what the effect of the tax is in its economic and political bearings.

The method of arriving at valuations of improvements has already been described, and it has been shown that they are surprisingly low, both in proportion to cost value, and also in propor-

tion to land value. The latter fact is, I think, for the interests of the community. It is desirable that improvements should be taxed at a lower rate than land, because while improvements are like land, in that they cannot run away, they are unlike land, in that they could and would come to a city under favorable tax conditions without which they might not come. It is not, therefore, on the ground that improvements are not as heavily taxed as land, that we would question the wisdom of the present system, but for two other reasons: first, the inequality of the present system; and second, the advantage to the political life of the city in the substitution of a tax which would make the cost of city government a matter of more immediate interest to a majority of its population.

I have already pointed out some of the inequalities of the present tax, and have shown that new improvements are assessed much more highly than old improvements, whether value be determined by cost, or by earning power. This is due to the anomalous conditions existing in New York, which lead New Yorkers to regard as temporary improvements edifices which in any other city would be regarded as good for a hundred years. As a result, we have old residences assessed at one fourth to one third of their cost, and new residences assessed at 80 per cent to 90 per cent. We have private residences assessed for less than the cost of their interior decorations, it being easy to secure an estimate of the cost of the unfinished building from the estimates filed with the building apartment, while it is practically impossible to learn the amount paid for interior fittings and decorations. The result is, of course, to place a much heavier relative burden on the tenement than on the palace, interior finish being a negligible amount in the tenement, while in the palace it is often as much as the building value proper. In the case of residences on extremely valuable land, if the rental value is taken into consideration in determining the improvement value, so much must be allowed for carrying the land investment that the remainder represents a very small capitalization in improvement. As a matter of fact, of course, in such cases there may properly be added to the rental value the expected return from the increment in the value of the land. Thus, a \$15,000 rental from a house on a lot assessed at \$250,000

does not necessarily indicate that the house is worth only a nominal sum, say, \$10,000, but that the owner anticipates that the rental will be supplemented eventually by land increment. Secondly, just as Philadelphia is celebrated as a city of homes, so New York is celebrated as a city of tenants, or occupiers, as they would be called in Great Britain. The number of those who own the homes they live in in New York has been placed as low as 10 per cent. The remainder, of course, pay rent. The great majority pay no direct taxes. The result is, there is utterly lacking even among the more intelligent part of our population any just conception of what they are paying for city government and municipal services.

It is a truism with students of municipal government that the interest of citizens is most easily reached through the pocket-book and that the only check on municipal extravagance and unwise municipal undertakings is a system of taxation which will convince the average citizen that he must foot his share of the bill.

On the other hand, a large body of social reformers who are more anxious to do for the people what they conceive to be good for them than to educate the people to demand what is best for themselves, would object to a tax which would increase the psychological sacrifice on the part of a large part of the community on the ground that it would prevent the carrying out of larger undertakings, which, however desirable they might be for the community, would be deferred and deferred from time to time because of their expense and the consequent increase in the tax rate. That this argument is not one to be ignored is evident from the fate that befell the new charter for Chicago. I am inclined to believe, however, that the delay and effort which are necessary in a democracy, which is founded on the principle that in the long run it is better for a man to govern himself, however badly, than to be governed perfectly by some other man, is worth what it costs, so that I question the ultimate wisdom of any form of taxation whose merits lie in the fact that the money is taken out of the citizen's change pocket without his noticing it. For these two reasons, I think the tax on improvements might better be levied in the form of a tax on rental values than in the form of a tax on capital value. In

other words one of these days when we determine in New York to do away with the present iniquitous personalty tax, and to increase the burden on real estate, I should be in favor of adopting as our system of taxation for a combination of the American and British systems, retaining our American system for unimproved land, but taxing city improvements according to rental values.

The arguments for the tax on rentals, which I shall hardly have time more than to mention, are:

1. Rental values are more readily ascertainable than the values of improvements and furnish, therefore, a more exact basis of taxation.

2. Rental values are a fair index of family income and a tax on rental values is, therefore, proportioned to ability to pay.

3. A tax on rental values permits the exemption of a minimum rental, say, \$100 a year from taxation, and if properly adjusted, would permit cheaper rents for the poorest class of dwellings or apartments.

4. A tax on rentals whether assessed against the occupier, as in Great Britain, or assessed against the owner, as is more desirable for the sake of ease of collection, would in its psychological effect be a direct tax for the majority of the population, and would give them an immediate concern in municipal expenditures.

New Yorkers are all alive to the fact that rents are very high in New York, but if you were to question a score of intelligent men, college professors included, as to what proportion of their payments for rent they thought went to pay the expenses of the city government, you would find their estimates wide of the mark. I imagine, therefore, that the proposal to introduce a tax on rental values of from 10 per cent to 20 per cent would appear at first sight as extortionate and an impossible burden, but in reality it would be no greater than the tax now paid indirectly. It must be understood, of course, that to reach the rental value of the improvement it would be necessary to deduct from the total rental value a sum sufficient to yield a fair return on the assessed value of the land, say, $3\frac{1}{2}$ per cent or 4 per cent net.

For illustration, let us take a lot assessed at \$50,000 with a house assessed at \$10,000 and renting for \$4000. The present tax is \$750 on the land and \$150 on the house. Allowing \$2500 or 5 per cent on the assessed value of the land, the rental value of the house would be \$1500, and a rental tax of 10 per cent would be required to yield the same amount as at present. Again, take a commercial building assessed at \$350,000, standing on a lot assessed at \$500,000 with rental value of \$50,000. It now pays \$7500 on the land and \$5250 on the building. If \$2500 were allowed as rental value of the land, it would require a tax of over 20 per cent on the remainder of rental value to yield as large a tax as at present. It is evident, therefore, that while the property would pay no more into the city treasury than at present, the psychological effect would be magnified, and the interest of the rent payer in municipal questions greatly increased. We should begin to understand that we were not so much better off with our present tax rates than our English cousins with their rates of two and three shillings on the pound, and we should begin to understand how some Londoners had begun to fear a rate of twenty shillings on the pound.

The objection may be raised against the proposed form of taxation that instead of diminishing it would increase the taxation of the poor, because the greatest gross rentals in proportion to the investment are paid by the poorest class of tenements. This, however, could be met in either of two ways: first, by a judicious exemption of rentals of small amounts; or second, by adopting certain fixed percentages to be applied to different classes of buildings to enable the assessor to estimate the net rental from the gross rental. To encourage the improvement of outlying property I should favor also the exemption from the tax on rental value for the first two or three years of both residential and commercial buildings when they were erected on property not previously improved. Many points would require careful consideration in the working out of such a scheme. The two arguments in favor of it, however: first, that it is proportioned to the surest index we have of income; and secondly, that it is psychologically a direct tax so far as the rent payer is concerned, whether paid directly by him or not, because it drives home the fact that 10 per cent to 25 per cent

of what he pays for rent goes for taxes, seems to me so strong and of such vital importance as to justify any temporary difficulty there might be in applying it.

With a tax on land and on franchises to bear the chief brunt of city taxation, a tax on the stock of certain classes of corporations, an excise tax, and a tax on the rental values of improvements, we should obtain, I believe, at least so far as New York City is concerned, all needed revenue, with the least hardship, and with the greatest justice and largest incidental political and social benefits.

THE TAXATION OF REAL ESTATE AND REAL ESTATE IMPROVEMENTS

BY F. A. DERTHICK

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THE theory of taxation of real estate and the improvements thereon is undergoing a change all over the world. In the beginning the wide stretches of unoccupied land had little or no value, and whatever of public burdens existed were of necessity placed upon goods, tools, stock and improvements. This was a tax upon industry and thrift, but was borne because the necessity was appreciated.

Along with the development of the country has come constantly increasing land values, until to-day land is the attractive target for the taxgatherer, the burdens of society having shifted in an important degree to the owners of land. In all the future land values will constitute an ever increasing volume of power as a burden bearer, and to this source of revenue the taxgatherer will return in every emergency, mount his beast of burden and spur it to the goal.

The sum total of taxes must always be forthcoming, and after every other source is exhausted the land must meet the deficit, be it large or small. This is the logical result of the fixed character: constant rise in value and imperishable nature of land, the source of all material life and wealth.

In determining the amount of taxes upon a given parcel of land, there are two main considerations:

First: Its natural resources — productivity, forest, mines, oil and gas.

Second: The degree in which a large or small number of persons desire that particular parcel of land for the erection of homes, sites for business houses, speculative purposes or any other cause.

This latter factor is frequently subject to rapid change, as cities are fickle in the direction of growth, often entering new areas, causing prompt advance in values there, with a corresponding decrease in the localities deserted or neglected.

This unequal and unexpected development, either in city or country, is often the cause of great injustice, as it confers new advantages upon those in the new district without increasing their burdens and at the same time decreases the values and profits of those in the old districts, without decreasing the burdens imposed.

This injustice calls for a more frequent appraisal of real estate than now prevails in Ohio and many other States. The assessor should be a man of unquestioned integrity and the salary be such as to command the best ability. With these provisions fully met, favoritism, incompetency and inequalities would be reduced.

Reënforce this provision by establishing the "District or Block System" for purposes of taxation, and whenever the taxpayer pays his taxes, supply him with a tabulated exhibit of the location, valuation and assessment of every parcel of real estate in his district. Upon receipt of this map, the taxpayer would at once compare his own with the valuation and assessment of his neighbor and promptly complain of any real or seeming injustice. This would make an assessor of every taxpayer.

Taken together these two provisions would go far toward reducing the present inequalities to the minimum. This proposition would be still more satisfactory were there a rigid separation of improvements from the land. The taxpayer would instantly compare his own with his neighbors' buildings and be able to say whether the respective valuations were just.

TAXATION OF IMPROVEMENTS

The taxation of improvements on land, especially buildings, is a question of an entirely different nature from the taxing of land. As before noted, in a rapidly developing community, land, without any effort by its owner, is carried forward to higher and still higher levels of value.

The case is different with buildings, as well as with many other improvements. When a dwelling, a business block or any other building is erected, it at once begins to deteriorate. When the last nail is driven, the last finishing touch given, that building is *one day* nearer repair. Sound economic principles would, therefore, suggest that improvements, being of a perishable nature, ought not to be subjected to the same valuation and rate that is placed upon land.

There is room for great difference of opinion concerning taxation of improvements, whether in country or city.

A young farmer enters upon the ownership and operation of land destitute of improvements, or with improvements of little value. He builds a home for his family, barns for his stock, adds fencing, establishes lawns, plants trees, cultivates flowers and at great expense and labor and money transforms what was at best but an unlovely place to stay into a beautiful, attractive home. The State immediately levies a tax as punishment on his energy, effort and higher ideals of what constitutes life. This is all wrong. No man liveth to himself alone. The total value of the property, as a whole, is increased, of course, and the valuation should be increased, but this pioneer in a community with low ideals should not be taxed to the full extent of his own thrift and sacrifice. Every tile intelligently laid, every extra bushel of products, every lawn, beautiful tree, fragrant flower, tasteful building erected, gallon of paint spread, adds to the value of not only his own farm but to the value of every acre of land in his community, and the community should contribute to the expenses of government in proportion to the benefit received; this for the encouragement of social and industrial progress.

This illustration can perhaps be made more graphic in the city. Within a few squares of the Statehouse in Columbus are vacant lots grown up to burdocks, briers and thistles, unlovely in appearance, each one a blot on the beauty all around. The owner will not improve nor sell to those who would. He is holding the lot which he bought for \$100 per acre until the energy, industry and sacrifice of his fellow-citizens enable him to sell at \$100 or \$1000 per foot. Every tasteful residence erected, lawn established, every flower that

sweetens the air, every tree that casts a grateful shade, every fountain that sparkles in the sunlight and every worthy citizen that dwells within the circle, all—all help to double, triple, quadruple, over and over the value of the unlovely lot across the way. Common justice and an enlightened public sentiment will one day insist that the vacant lot shall share in larger measure in the expense that has contributed to its own enhanced value.

It would seem that some law, usage or system should so instruct assessors that they would recognize the perishable nature of improvements as compared with the stability of land; also the importance of improvements as a factor in advancing the value of adjoining unimproved land held for speculation.

If any one fears for the revenues because of this suggested leniency for improvements, he has only to become acquainted with conditions in very many parts of the country. The limits of this address will not allow statistics from a wide range, but possibly one instance will be permitted. On what is known as the "Macy Corner," 34th and Broadway, New York City, is a lot 31 feet $10\frac{7}{8}$ inches by 50 feet $6\frac{3}{4}$ inches, which is assessed on a valuation of \$330,000 aside from improvements. This building is valued at \$15,000 and the property rents for \$32,000 per year, or the interest on \$800,000 at 4 per cent. A little mathematics show that this *site*, without the building, is valued by the city at \$10,000,000 per acre.

There is land in New York City valued at \$40,000,000 per acre and the value of *site* in each instance given is being carried forward to still higher planes, not by any effort of the owners, but by the sheer momentum of the life and business that throng around them. There seems to be no cause for fear for our revenues, so long as we have this princely heritage—the *land*—its opportunities and resources. It must not be supposed, however, that because I have insisted that the collection of taxes from real estate is easy and certain, I am in favor of releasing from taxation any other form of private property, tangible or intangible.

I believe that all citizens should contribute to the support of the state and local government in proportion to the income

from their property, whatever its nature. There is sufficient wealth in most States, in Ohio certainly, to meet all legitimate expenses, without distressing anybody, were all property on the duplicate.

The tax duplicate of Ohio is about two billions. There is no doubt but this should be reënforced by at least a billion dollars of what is recognized as intangible property. To withhold one third of the property of the State works a gross injustice upon the holders of visible property, among whom are the farmers.

Instances might be multiplied to prove that our intangible property is not returned for taxation. One case only is given. In 1905 the return of personal property for taxation in Cuyahoga County, O., was \$62,000,000. This included all of the 20 townships of the county, the farmers' flocks and herds, implements and personal property of every description, together with the city of Cleveland. In that same year the banks of Cleveland by official announcement in compliance with law showed their deposits to approximate \$300,000,000. Why was not this large amount, supplemented by the many millions of other forms of intangible property, on the tax duplicate? Tax experts are saying to-day that it was because of the fallacy of the uniform rate upon all property at its true value in money. If this be true, and all history proves it, it would seem that the first step in an effort to harmonize the tax laws of the various States and relieve real estate from excessive taxation would be to eliminate the uniform rate by amending our constitutions.

It is claimed by some that "taxation is compulsory." This may be true in case of tangible property, but the moment the assessor enters the domain of intangible property, it is all a farce. There is, save by accidental discovery, no compulsion possible. The tax on intangible property instead of being compulsory *is a tax on conscience.*

It has always been true, and always will be true, that when the tax rate in any zone of taxation exceeds, equals or approaches the net income from intangible property, it will hide, no matter how severe the burdens may fall upon the holders of tangible property in consequence.

The tax rate of municipal districts in Ohio to-day averages $3\frac{1}{2}$ per cent. The banks of Cleveland pay 4 per cent on deposits. The tax rate in Ottawa, Ohio, is \$4.40 per hundred; banks pay 4 per cent. How can a taxpayer live in either city, if his money is on deposit there, and be honest? He must do one of three things: move out of the district, change his investment, or commit perjury. Experience proves that he does all three. 'Tis true that it is too bad that such conditions exist, but 'tis too bad it is true that they do exist, and that public opinion condones the perjury, for public opinion will never countenance an injustice. That same public opinion would instantly rebuke a taxpayer who refused to contribute a reasonable part of his income to the support of government. The question of taxation is not only a social and economic question, but is a moral question as well, and all laws bearing upon the subject should recognize the moral aspect of the case.

The contention is that a taxpayer who would not return his property at a rate that would absorb the larger share of the income, would return it at a low rate for the sake of a clear conscience and safety from the full rate, with penalty added. If a rate of one half of 1 per cent instead of $3\frac{1}{2}$ per cent were granted in Ohio, and in consequence the billion dollars of intangible property estimated to be withheld were brought to the duplicate, the income would be \$5,000,000 annually, something that we never had before. This vast amount would build 12 miles of stone road in every county in Ohio each year. It would pay one hundred and eighty-five teachers \$40 per month for eight months in every county in the State. It would be like having something given to us without loss of anything we had before.

It is claimed in certain quarters that a low fixed rate will yield no more revenue than a high rate, and for those who think that owners of intangible property will withhold it from taxation as certainly under a low rate as under a higher, I will give below the substance of a letter received under date of September 28, from Judge Oscar Leser of the Appeal Tax Court, Baltimore, Md.

"In 1896 Maryland introduced a new system in the taxation

of foreign and domestic companies, and the shares of stock of foreign companies. Up to that year these forms of property were subject to the full, direct state and local property tax at their actual value. The Act of 1896 substituted a tax of three tenths of 1 per cent on the assessed value for local purposes, but did not change the state rate. Our figures show that in 1896, the last year in which such securities were taxed at the full city rates of about \$2 per \$100, there were found \$6,000,000 yielding a revenue to the city of Baltimore of \$120,000. Under the new three tenths of 1 per cent tax law, the securities returned for taxation amounted to \$55,000,000 with an income to city of \$165,000. Since that time there has been an annual increase in such securities, so that for the present year (1907) there are \$150,000,000 on the books, while the city's revenue from this source is nearly four times as great as ten years ago under the high rate." (Approximately half a million under low rate against \$120,000 under high rate.)

Continuing, the Judge says: "In 1896 the tax collected by the State on securities in Baltimore City was about \$10,000. Ten years later the income to the State was twenty-five times as great. The new law has produced highly beneficial results. It has largely taken away the incentive to perjury on the part of the taxpayer, and it has encouraged the investment of money in taxable securities, while at the same time a substantial revenue has been vouchsafed the city and State. It can readily be seen that the *moral effect* of such a law has been highly beneficial. In an indirect way it has stimulated honesty in other matters affecting taxation. Public opinion fully supports the new law, and frowns upon any attempted violation of it."

It will thus be seen that by cutting down the local rate six and a half times, the local revenues were increased 400 per cent while the state revenues were increased 2500 per cent. This also shows that it is not the small state rate to which taxpayers object. Some there are who so revere constitutions that they object to change, yet have long since turned from their yoke-fellows.

When the constitution of Ohio was adopted, the sickle, the scythe and the cradle were indispensable on the farm, but they have given place to the mowing machine and twine binder.

The canal boat, the flail and the ox-cart marked the era when our constitution was framed, but all have been succeeded by modern inventions. The little red schoolhouse has in all the past been the bulwark of our free institutions, but is rapidly yielding the palm to the centralized schools. The old oaken bucket touches a tender chord in all our hearts, but it exists in sentiment only. The uniform rate served its day and generation, but with all the others is outgrown. Let every State throw it overboard and join in the march toward better things.

I would place no details as to taxation in the constitution beyond the bare statement that taxes should be justly assessed and collected for the benefit of the public. The people may be trusted to work out the problems as to what constitutes property, double taxation and a hundred kindred questions. The whole subject of taxation should be assumed by the people, who through their representatives, assisted perhaps by a non-partisan commission, may devise a system of taxation that will enable each generation to meet the conditions that exist when their turn comes.

Stated in specific terms I believe that the tax clause in our present constitution is outgrown and that now there should be placed in some department of the governmental structure of each State directly responsible to the people the power to revise our tax system from time to time as conditions, necessities and experience suggest.

MUNICIPAL TAXATION OF INTANGIBLE WEALTH

By PROFESSOR JACOB H. HOLLANDER

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THERE is a depressing uniformity in the financial condition of American cities: restriction and retrenchment in expenditure, inelasticity and insufficiency in revenue, increase and strain in indebtedness.

The reasons for these conditions are as familiar as the conditions themselves. The American city is being called upon, not only to do new things, but to do the old things in a more costly way. It is probable that at best municipal service is subject to what economists term "the law of increasing costs," but this principle is tremendously heightened in effect by popular insistence upon new and expensive methods, tending to more efficient performance and larger social comfort. Not only does it cost more to pave or light a larger or more populous city, but a better type of lighting and costlier forms of paving are imperiously demanded.

The point of maximum pressure is the municipal tax rate. Up to a certain point the city may restrict further expenditure, or indeed effect positive retrenchment. But new school-houses must be erected, more engine houses must be supplied, a larger police force must be maintained, and so-called developmental functions must be expanded — all working out to the steady and uninterrupted growth of the municipal budget. It is true that more enlightened municipal policy seeks to increase revenue from sources other than direct taxation. A rational course with respect to industries of service means larger income, without either the neglect of *laissez faire* or the unknown sea of municipal ownership. A saner attitude toward the retail liquor trade involves substantial gain to the municipal treasury, to the benefit of civic ethics and public morals. So, too, a larger use of special assessments and a more sagacious policy with respect to suburban areas present further opportunities for fiscal improvement.

But increasing municipal needs more than absorb the financial gains here effected, and after all has been said and done, the typical American city is driven back to the necessity of supplying the largest part of its present and prospective requirements by the direct taxation of property. Short of some radical and unlikely change in constitutional restrictions and municipal organization, the direct taxation of property must continue to be the mainstay of the American city's budget.

In so far as property, as here employed, means real estate, that is, land and improvements, there is no serious divergence between the experience of practical administrators of municipal affairs and the opinion of careful students of municipal economics. The sentiment of both is in accord with the recent dictum of the distinguished Vice President of this convention, that the equitable assessment of real estate is the very foundation of the city's credit and the basis of its economic welfare.

As a matter of fact, no phase of American municipal administration has been more negligent and culpable than the assessment of real estate for purposes of taxation. From mistaken economy and a well-intentioned but utterly inexpert personnel at best, we have run the gamut to political appointees, party pressure, gross favoritism and outright corruption at worst. Explicit provisions of law have been neglected or violated, and for the simple workable devices of full assessment and continuing revision we have had arbitrary valuations aggravated by spasmodic raids.

The developments of the last few years have seen change for the better in these directions. Thanks to the notable example set by New York City and the continuing campaign of enlightenment of which a meeting such as this is the tangible expression, public sentiment and municipal administrators are rapidly agreeing that whatever conditions may prevail elsewhere, the assessment bureau is the one branch of municipal administration which must be conducted, in the matter of personnel and practice, on the most rigid business principles, and that, in these days, the American city may not indulge in the luxury of using in any degree its assessment department to strengthen political ties or to discharge political debts, or

to do anything else but to assess property and to assess it correctly. Progressive municipal administration, no less than a more enlightened public sentiment, insist that a continuing revision of real estate, which will, without spasmodic dislocation and jar, keep the assessed valuation of land and improvements in close correspondence with actual market value, means substantial relief to the municipal treasury and greater equity to the municipal taxpayer, and that this result is no remote ideal, but as practicable and obtainable a state as any phase of efficiently conducted private business.

But the problem of personal property we still have with us — or at least that part of it which figures in fiscal discussion as "intangible wealth." The assessment of chattels and household effects, of mercantile stocks and industrial plants, of shares of stock of domestic corporations, and of locally employed capital of foreign corporations, present difficulties not different in degree from the efficient valuation of real estate. It is when we leave the domain of things and come to the realm of rights, and have to do with stocks, bonds and evidences of ownership not taxable "at the source," that the real difficulties occur. For here it is no longer the relatively simple elements of finance that confront us, but an intricate complex of finance and psychology — escape from taxation, double taxation, jurisdictional conflicts.

So flagrant have been the lapses of intangible property assessment, and so complete has been the breakdown of insistent attempts to associate intangible wealth with real estate and tangible personalty for identical taxation under the term "general property," that the pendulum of expert opinion has tended to swing to quite the other end, and some of the most distinguished students of American finance have urged the complete exemption of such intangible property, and, as a means to that end, the separation of state and local sources of revenue, by constitutional amendment and legal enactment, in so far as necessary.

It is hardly necessary to insist that these two proposals are in essence independent and distinct, and that although the provisions of the ordinary American state constitution would prevent the exemption of personalty, save as a corollary to the disso-

ciation of state and local revenue, yet it by no means follows that the converse is true, and that advocacy of such separation carries with it a necessary presumption in favor of exempting personalty.

Indeed, at this point expert counsel and public opinion have been in sharp opposition. The text-book writers have accumulated masses of graphic evidence of the inherent depravity of the tax on intangible personalty, and have insisted on its complete elimination from the scheme of local taxation. On the other hand, public sentiment has been unwilling to tolerate the concrete fact of wealthy citizens, owners of stocks and bonds, enjoying all or many of the benefits of municipal service, and freed entirely from the onerous tax burden resting upon other forms of property.

I do not propose, in this connection, to discuss the relative merits of these opposed views. Much has been left unsaid on both sides. Certainly not a fraction of the actual evils attending the working of the tax on intangible wealth has been brought to light. But on the other hand its critics have made sad confusion of theory and practice, of principle and administration, and have cried out somewhat dramatically that the tax is bad, because attempted under hopeless conditions, it has worked badly. More than this, insufficient emphasis has been placed upon the fact that an equivalent *burden* of taxation upon different classes of property does not necessitate an identical *rate* of taxation. Wherever, as in the contrasting cases of real estate and intangible wealth, tax liability on the one hand and tax immunity on the other — as represented by many years of actual tax administration — have been virtually capitalized, fiscal justice is approximated, rather than violated by differential rates.

Leaving aside this fundamental analysis, tempting as it is, my purpose at this time is the practical one of describing the manner in which one particular city, Baltimore, has undertaken to solve the problem so presented, and to intimate to you the results which have attended this attempt.

The reckless participation of Maryland in various schemes of internal improvement in the decade from 1830 to 1840 resulted in the accumulation of a large and oppressive state debt. Direct taxation, hitherto distinctly an emergency resource, became in

1841 the only means of averting repudiation. The imposition of a general property tax was proposed, resisted, delayed and finally effected by the passage on April 1, 1841, of "an act for the general valuation and assessment of property in this State, and to provide a tax to pay the debts of the State." It authorized the first general reassessment of property in Maryland since 1812, and imposed a direct property tax for state purposes of one fifth of 1 per cent.

In Baltimore, the Act of 1841 interrupted the logical development of a system of local assessment along the lines projected by municipal legislation in 1836-1839, and introduced the essential features of the modern property assessment system of Baltimore, viz. the employment of a common basis for state and municipal taxation, and the virtual absence of any periodic local reassessment or continuing revision. Subsequent general revaluations of property primarily for purposes of state taxation were made in 1852, in 1858 (in Baltimore City), in 1866, and in 1876.

The results attained in Baltimore by the reassessment of 1876 remained practically the basis of local taxation for the next twenty years, during which time occurred no general revision of valuations. The resulting conditions were exactly what might have been expected from an original faulty assessment and a long period of neglected revision: the widest discrepancies in rate and manner of assessment as between county and country, and as between counties and city, and the most intense resentment at the evident escape of personalty.

In the legislative campaign of 1892, reassessment was made a successful party issue. The general assembly then elected promptly passed a radical reassessment law, of which the conspicuous feature was drastic provision for the listing of personal property. But so bitter was the outcry raised by propertied and mercantile interests in Baltimore City and throughout the State, that after a brief period of indecision, the Governor vetoed the measure. Reassessment slumbered in 1894, but two years later the forces were again marshaled and the long-deferred revision was authorized.

This time the crucial point was met by simple compromise. Provision was made for a stringent though less drastic listing, and for biennial relisting. The bonds and certificates of in-

debtedness of all corporations and the shares of stock of foreign corporations were assessed at their actual market value and subjected to the full state tax of $17\frac{1}{2}$ mills, as all other forms of taxable property. But in lieu of the ordinary municipal and county taxes, varying in rate from 60 mills to 2 cents, a fixed maximum charge of 30 mills or three tenths of 1 per cent was imposed for local purposes upon property so listed.

The motive of the adjustment was evident. County sentiment stood for a rigorous listing of personalty, and fortified its position by the declaration of the Maryland constitution of 1867 that "every person in the State, or person holding property therein, ought to contribute his proportion of public taxes for the support of the government, according to his actual worth in real or personal property." City sentiment, willing enough to take its chance with the old assessment law, but fearful of the severities of the proposed new law, stood firm in opposition, insisting that rigid listing meant either a greater premium upon perjury or the quick expulsion of local capital. In this juncture, imposition of the full state rate and a moderate maximum for local purposes was suggested as a fair compromise, and to it both parties assented — rather than incur the risk of a second executive veto or the ultimate passage of a drastic measure.

Turning now to the actual operation of the tax, attention may properly in this connection be confined to Baltimore City. There are several reasons for this, aside from the very practical one that only in the case of Baltimore are sufficient data available. In the first place, we are primarily concerned with the usefulness of the measure in a scheme of municipal taxation. Moreover, Maryland is distinctly an agricultural State of moderate accumulated wealth, and the only other local divisions likely to contain appreciable amounts of securities are Allegheny and Washington counties, in which Cumberland and Hagerstown are respectively located, and Baltimore County, whose salubrious climate and lower tax rate have induced numerous wealthy persons engaged in business in Baltimore to acquire legal county residence. Finally, the method, or utter lack of method, of county assessment is so defective as to throw no helpful light whatever upon the merits or defects of the tax itself.

The reassessment of 1896 resulted for Baltimore City in a

return of \$58,703,795 of securities.¹ Upon this was imposed 17½ mills (the full state rate) for state purposes and 30 mills for city purposes. In 1898 the total was slightly revised to \$60,699,686. The biennial relisting, provided by the original measure, took place in 1898. It proved so complete a failure — the basis rising only to \$61,890,764 — that it was repealed in 1900, and in lieu thereof the appeal tax court (the municipal assessing board) was charged with the duty of continuous valuation and quinquennial revision.

The total assessed valuation of securities returned for the 1899 basis as \$61,000,000 rose in 1900 to 65,000,000; in 1901, to 68,000,000; in 1902, to 89,000,000; in 1903, to 94,000,000; in 1904, to 85,000,000; in 1905, to 104,000,000; in 1906, to 120,000,000; in 1907, to 150,000,000, and in 1908, to 146,000,000. The precise figures are as follows:

1897	58,703,795	1903	94,336,562
1898	60,699,686	1904	85,971,333
1899	61,890,764	1905	104,221,227
1900	65,789,903	1906	120,423,814
1901	68,879,484	1907	150,947,733
1902	89,880,484	1908	146,688,857

It will thus be seen that in the ten years of its operation, the taxable basis of intangible wealth, subject to the flat local rate of 30 cents, has increased from \$58,703,795 to \$146,688,157, or roughly, 150 per cent. If the errors of the original assessment and the abnormal depreciation in securities of the last few months be eliminated, and comparison be had between the \$58,000,000 of 1897 and the \$150,000,000 of 1907, the result is a round increase of 170 per cent. During this same interval of ten years, the total assessed valuation of other forms of personalty, excluding shares of stock of domestic corporations, but including tax-exempt manufacturing plants, increased only from \$37,020,838 in 1898 to \$39,232,866 in 1908, or 6 per cent. The movement in real estate during this same period was from \$233,955,093 in 1898 to \$325,723,818 in 1908, or 39 per cent.

¹ From the limited data available, it appears that for the year prior to the reassessment of 1896, securities — then liable to the full property tax — were returned in Baltimore only to the aggregate amount of \$6,000,000.

But an appreciable part of this more favorable showing was due to the unusual activity of the appeal tax court in revising real estate valuations in the last three years. If the basis of comparison be made from 1897 to 1904 so as to exclude this period, the results show an increase of 46 per cent in securities and 9 per cent in real estate.

While the results thus obtained have been absolutely substantial and relatively favorable, they by no means represent maximum possibilities. During the period under consideration, Baltimore suffered a devastating conflagration, involving the destruction of many millions of tangible property and the necessary liquidation and conversion of considerable holdings of securities. The whole system of capital holding was disorganized, and only during the last two years has anything like equilibrium returned.

Moreover, the assessing force, although a substantial improvement over the older conditions, leaves much to be desired, both on the score of numbers and expert equipment. The whole basis now upon the tax books, exclusive of the original listing, represents little more than the reasonably diligent efforts of a single man working upon the problem at hand, under intelligent direction, but without either special equipment therefor or systematic plan in pursuit. I have no hesitation in saying that not only are better results attainable, but more than this, that any conceivable kind of tax would work poorly if similarly handicapped in administration. That under these conditions the results have been so favorable confirms the fiscal possibilities of the measure at its best.

While the results, from the standpoint of the city's treasury, have thus been far from unsatisfactory, the operation of the law has met with as much favor at the hands of security holders as any form of personal taxation may expect to receive. That it is preferred to the old farcical endeavor to subject all such property to the full city rate goes without saying. That it is deemed a not unfair operation of the municipal burden is perhaps too much to state. But all things considered, there seems a reasonable content, based in part upon appreciation of its necessity, in part upon fear lest it might be replaced by a worse substitute.

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Whatever timidity operates to prevent a fuller return of securities seems to be inspired less by discontent with the burden of the present rate, than the concern lest, when such property has been once assessed, the flat rate be repealed and the full city rate be imposed. In confirmation of this anxiety, the well-known example of Connecticut in dealing with a somewhat similar device has been exploited. But, on the other hand, public sentiment seems to be crystallizing, not only in favor of the tax as now imposed, but even to the point of recognizing that a breach of faith, or certainly a departure from sound policy, would be involved in any such change. At this juncture such a change is so remote as not even to be bruited, and from year to year, as the tax becomes more firmly entrenched, and its results more favorable, the chance of any such course is likely to grow even less.

In short, Baltimore, ten years ago, through practical exigency rather than in consequence of scientific analysis, adopted a method of taxing so-called intangible wealth which, in the decade of its operation under but fairly efficient administration, has placed a steadily increasing assessment upon the tax books, to the material betterment of the city treasury, to the appreciable relief of the overtaxed real estate owner, to the manifest improvement of local tax morality, and to the lessening of county immigration for tax purposes. There is no serious dissatisfaction with the operation of the device on the part of those directly affected, and there is expectation that by keying up the whole tone of municipal tax assessment, substantially better things can hereafter be achieved for the city's interest. Subsequent experience may reveal defects or fallacies not now evident, but if such be the case, amendment or repeal are entirely practicable. Considered as nothing more than a piece of fiscal opportunism, the Baltimore device can properly engage the attention of such similarly circumstanced communities as, convinced of the un wisdom of further blunderbuss attempts to assess intangible wealth for full property taxation, are not yet prepared to go to the other extreme of complete exemption. To these the method here briefly described has, to the limited extent of its application, at least the merits of reasonableness in theory and a fair amount of success in practice.

REFORM IN MUNICIPAL TAXATION

BY PROFESSOR CHARLES EDWARD MERRIAM

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NOWHERE are the bonds of an antiquated or obsolescent taxing system more quickly and more keenly felt than in the modern city. Here the most advanced phenomena of modern industrial life are seen, and here the difficulties of adapting old laws to new conditions are earliest apparent. I listened last summer to an animated debate in the House of Commons on the taxation of site values; in Germany I found the subject of the "unearned increment" a burning question; and I returned to Chicago to find many citizens objecting to an increase of taxation without an alteration of the system. Since the present system of taxation was designed for rural communities under relatively primitive conditions, the evils arising under complicated urban situations are inevitably acute, and indeed almost intolerable. Only a highly dynamic condition of industry and commerce, in a period of unusual indifference to scientific legislation and expert administration, can explain the continuation of a system so cumbrous and defective. However, the increasing expenditures of municipalities, the growing attention to economic and political problems, and the constantly greater difficulty experienced under the present system — all indicate movement in the direction of reform in the immediate future.

Conspicuous among the evils of the present municipal situation is the general property tax. Under early agricultural conditions, where almost all property was visible and tangible or where loans or credits could readily be ascertained, this form of tax was not objectionable. But under urban condition, and especially under modern industrial conditions, where immense values are neither tangible nor visible nor easily ascertainable, the system becomes unworkable. From the viewpoint both of economics and politics, this tax is a prolific source of inequality and injustice. Repeated investigations have piled up moun-

tains of evidence against the economic injustice of this system until it would seem that every intelligent citizen, if not already informed by personal experience or observation, must be familiar with the scientific demonstration. "The general property tax sins," says Professor Seligman, "against the cardinal rules of uniformity, of equality, and of universality of taxation. . . . It presses hardest on those least able to pay; it imposes double taxation on one man and grants entire immunity to the next. In short, the general property tax is so flagrantly inequitable that its retention can be explained only through ignorance or inertia." The citizen of moderate means suffers because he bears far more than his share of the general burden; while the rich suffer from the uncertainty of the valuation and its liability to extreme fluctuations, and from the inequalities existing between various industries or individuals.

Attempts to enforce this law have invariably proved futile. Drastic methods of every description have been tried repeatedly, but with the same inevitable and unvarying result. Even the tax inquisitor, or tax ferret plan, under which county boards are authorized to contract with private detectives for the discovery of property unreturned by the owner, has resulted in little more than an extensive practice of blackmailing. Indeed, the general effect of increasing the stringency of personal property laws has been an increase of evasiveness and deceit rather than of valuations and of revenue. The common assertion that the general property tax needs only vigorous administration to insure its success is based upon ignorance of the experience of American States and cities during the last generation. In the case of cities, the difficulty of enforcement is made even greater by the ease with which the citizen, in case of a valuation regarded by him as "excessive," may remove beyond the corporate limits to districts where both valuation and rate will be more satisfactory. In short, the complete or even approximate enforcement of the general property-tax law, so far as urban communities are concerned, is an administrative impossibility.

The objections to the general property tax are both economic and political, however. Ordinarily, the economic objections are urged against it, but the political difficulties and abuses are equally significant. Indirectly this form of a tax exercises a

morbid influence over the community by its tendency to necessitate, or at least to facilitate, evasion and deception. Considered in this way, it is really a subtle poison which exerts a most baneful influence upon the entire body politic. No community can pass through the annual process of tax dodging and remain on the same plane of political ethics as before. No more ingenious method for wholesale debauchment of the electorate was ever embodied in the institutions of any State in any period of history. So far-reaching is the effect of this process that it has been known to result in the demoralization even of those most keenly and actively interested in political reform. Indirectly, then, the influence of the personal property tax upon the political life of our cities is injurious to an extent appalling to contemplate.

Directly considered, this antiquated system of taxation results in the most serious political evils. In many of our urban communities, the personal property tax is a strong bulwark of the organization. This law makes it possible either to grant entire immunity to favored individuals by failing to assess, at proper value, their property, or to inflict upon other less favored individuals a valuation which amounts to something approaching confiscation of their property. There are, of course, all possible degrees of laxity and severity between these wide extremes. To place in the hands of a political machine the power to tax or exempt from taxation millions, or hundreds of millions, of taxable property, under a system where accuracy of valuation is almost impossible, is folly of the most monumental character. Administrators of tax laws are only human beings, and they cannot be expected to rise above human nature. This control, then, over the taxation of property places tremendous power in the hands of a political organization, and is undoubtedly exercised in very many cases for the purpose of maintaining the authority of the dominant group. Even where this power is not exercised in its boldest form, its indirect influence is of very considerable importance. It smoothes the way for campaign contributions; it often gives the stoutest opposition pause. It appears, then, that the political evils resulting from this tax are of equal importance with the economic disadvantages. The political relief experienced by the abolition of the general

property tax is just as important to the community as the relief obtained from the unfair and unequal economic burden.

It would not be possible, however, to abolish this system for the personal property tax without providing an adequate substitute. It is at precisely this point that the greatest difficulty has been experienced. While it has been comparatively easy to secure general agreement upon the undesirability of the personal property tax, yet it has not been found possible to unite in any general movement in favor of any particular substitute. Various plans have been urged from time to time, and the most important of these possibilities will be briefly examined here.

An elaborate system of licenses for various occupations is in vogue in many of the Southern cities of the United States and in European countries. The occupation from which the largest amount of the revenue is derived is the liquor business, from which an increasing sum is received in American cities. This license is imposed both for police and revenue purposes, but it is not likely that it will be increased materially in the large cities, where the general rate is now from \$1000 to \$1500 a year.

Another special form is the mercantile license of Philadelphia and St. Louis. In the former city, where the personal property tax is only 40 cents per \$100, there is a special tax or license based on the volume of business transacted annually by dealers in merchandise. Retailers pay at the rate of \$1 per \$1000; wholesalers, at the rate of 50 cents per \$1000; exchanges and boards of trade, at the rate of 25 cents per \$1000. From this source about \$350,000 is collected annually; but this amount goes to the State, and the city has no share in it. In St. Louis there is a merchants' and manufacturers' special tax and license. On merchandise and on manufacturers' material there is a tax of 92 cents per \$100 (regular tax 2.19, 1904), and on the gross sales a city license of \$1 per \$1000 is required. Thus a merchant having a stock of the value of \$10,000 and sales of \$50,000 will pay on the stock a tax of 92 cents per \$100, or \$92, and on sales a license fee of \$1 per \$1000, or \$50, a total of \$142 tax and license.

While it would be possible to raise large sums of money in this way, it is not likely that very large revenues will be derived in the future from licenses. Such systems are likely to be complicated

in construction, expensive to administer, often irritating and vexatious in operation, easy of evasion, and likely to be unequal or unjust in their incidence. Where particular occupations are subject to license primarily for police purposes, incidental revenue will also be derived; and it is probable that the number of such special licenses will increase as time goes on; but it does not seem likely that such licenses will be made a proportionately larger item in municipal revenue. They cannot be regarded as adequate substitutes for the personal property tax.

Compensation for franchise grants to public service corporations, such as street railways, gas, electric light, and telephone companies, might, if desired, be made a source of profit to the municipality. Car licenses, lump sum payments, street paving requirements, and percentages of gross or net receipts are among the methods of securing such compensation. For a time it was thought that such receipts might be employed to defray a considerable part of the expense of government, and thus to relieve the pressure of taxation. More careful analysis has shown, however, that such revenues are, in reality, forms of indirect taxation bearing unfairly and unequally upon the economically weak. The working man or woman, on a small wage, pays not only a proportionately higher share of income, but a higher gross sum than the man of millions, in the case of a street railway fare, while the same principle holds good, in less degree, in regard to gas and electricity. Revenue obtained in this way bears, therefore, too heavily on those who are least able to support its weight, and is not a desirable form of permanent income for a municipality. Compensation should take the forms of lower rates of service, or an improved grade of service, and should not be employed to cover general expenses of government. Such services should be furnished at a figure covering all items of cost, including a reasonable profit in the case of private ownership. In Chicago it is proposed to apply the city's share of the net earnings of the street railways to a sinking fund for the construction of subways or for the ultimate purchase of the system.

The Massachusetts Commission of 1897, of which Professor Taussig was a member, strongly urged the adoption of the habitation tax. A section of the New York Tax Commission of 1907, including Professor Seligman, has recently proposed it; and in the

writer's report to the Chicago City Club on municipal revenues in 1906, this form of tax was suggested. The theory upon which this tax rests is that rental value measures, roughly speaking, the income of the occupant. Low rentals under this system would be exempt altogether from the operation of the law, and a progressive rate would be applied as the amount of the rental increased. The New York Commission proposed to exempt rentals from \$200 to \$600 a year, according to the size of the city, while the Massachusetts Commission proposed the exemption of rentals to the value of \$400. On the excess over this amount, the New York Commission suggested a rate of 3 per cent with a sliding scale advancing to 20 per cent in the case of rentals amounting to over \$20,000 a year. The Massachusetts Commission proposed a rate of 10 per cent without any progressive features.

The advantages urged in favor of this form of tax are that it would be much less easy to evade than the present personal property tax; that the administration of such a law would be comparatively simple; that the burden of the tax would not be oppressive and that the incidence of the tax would not be unfair. Evasion of such a tax would be manifestly difficult since the rental value of the property may be easily ascertained by the assessor, even if not voluntarily given by the occupant. Removal to cheaper quarters at a lower rental is not likely, since reduction of the amount expended for rent is one of the last economies which the average individual will make. For the slight additional amount of tax required, it would, furthermore, be scarcely worth the difficulty and expense of removal. The exemption of the lower rentals accompanied by the graduated increase as the rental value rises would distribute the burden of taxation with approximate equality. Such graduation would be necessary since the percentage of income expended for rent tends to decrease as income increases. It is evident, of course, that the working man spends a much larger percentage of his income upon rent than does the millionaire, and unless some such adjustment by means of graduation were made, the incidence of the tax would be wholly unfair and unjust.

As a revenue producer, there can be little question that the habitation tax could be made to yield much larger returns than

the present personal property tax without the accompanying features of fraud and unfairness that are now inseparable from the latter. As a substitute for the personal property tax, then, there are strong considerations that may be advanced in favor of the habitation tax. It combines the elements of equity and ease of administration, and makes possible the collection of the considerable sums necessary to meet the growing expense of American cities. The question of a habitation tax should be carefully studied in its administrative, political and economic bearings with a view of substituting it for the present personal property tax. It should be borne in mind, however, that no satisfactory solution of this problem can be reached without considering the municipal revenue system in its relation to the state system. Under a reorganized state revenue scheme, it is probable that personal property will be reached also by corporation taxes, by inheritance taxes, or by a national income tax even; and the extent to which it is so affected must necessarily be considered in connection with the adoption of the habitation tax.

Waiving the question of the particular kind of tax to be substituted for the general property tax, it is urged that state and local systems should be separated so that the urban community need not be bound up to the system of the rural community. Segregation of sources of taxation, a topic elsewhere considered in this Conference, is familiar to all students of finance and is found in practice in varying forms in Pennsylvania and various States.

In some cases an effort has been made to secure specific sources of income for the state government, as corporation taxes, inheritance tax, liquor license, leaving to the locality other sources such as real estate, license and fees. Another plan, adopted in Oregon, is the apportionment of the burden of state revenue among the counties on the basis of county expenditures. It is contended that the first of these two systems is rigid and inflexible, while the Oregon plan affords greater elasticity and, furthermore, that it enables the locality to follow more closely the range of state expenditures.

Whichever of these plans may be demonstrated to be superior, it is clear that the city should not be tied down to the objects of

taxation of the rural community. A system of taxation must be flexible enough to adapt itself to varying conditions. Without such statutory and constitutional changes as are necessary to make this possible, the development of an equitable tax system in a modern city is practically out of the question. Whether we favor a modification of the personal property tax, or the habitation tax, or the single tax, it is clear that substantial progress cannot be made, so long as the proposed system must be made to fit both farming land, horses and cattle, and metropolitan streets, stocks and bonds.

Turning to the valuation of real property in urban communities, we encounter serious difficulties. The rapid rise of values in some neighborhoods, the decline of value in others, the shiftings and changes in the character, uses and desirability of considerable areas, inevitable in the phenomenal growth of the modern city, make a proper appraisal far from easy. Both honesty and intelligence in high degree are necessary in every part of the taxing force. The valuation should be made, in the first place, with absolute honesty of intention, and, in the second place, with scientific precision and accuracy of method. At present, it cannot be said that the public always enjoys the benefit of both of these requisites. The valuers of property are, in only too many cases, political appointees who are the tools of their superior officers, and their valuations are the product of political expediency rather than of exact observations of real estate conditions. Furthermore, assessors are often employed for part of a year only, and are not occupied continuously enough to acquire the necessary facility in valuation. It may seem to be economy for a community to employ for two or three months in the year a swarm of men poorly paid to pass upon the value of millions of property, but, from another point of view, this is the worst sort of extravagance. It is imperatively necessary, in the first place, to have men of less dependence upon political organizations, and, secondly, to give them a permanent tenure of office and a salary proportionate to the value of the services rendered. By providing a system of rotation in assessment, as in Toronto, valuers might pass from district to district and spread the work over an entire year. In this way, the same set of men would be continuously engaged in the expert work of

real estate valuation. At the end of one year or two years, having completed the valuation of the city, they would begin again. A system of this kind would have the effect, furthermore, of relieving the congestion often experienced by boards of revision or review of valuation, and would also facilitate the work of tax collection.

The election of city tax officials is a feature of the local tax system that should speedily be abolished. There is no sound reason that can be advanced why a purely administrative officer of this type should be chosen by popular vote. The assessor is no more properly a subject for election than the city engineer or the city statistician. There is no such thing as a Republican assessment or a Democratic assessment, but solely an expert and honest valuation. There can be no difference of opinion between the two parties as to the nature of the assessment, or there should be none, if the law is to be uniformly enforced. The people elect the legislators who determine the general scheme or policy of taxation, but the execution of this plan should properly be left to appointive administrators. Choice of tax officials, as in Denver, Chicago, St. Louis or San Francisco, does not increase but really diminishes actual popular control over the tax authorities.

To summarize: the most urgent need of the municipal tax system is the abolition of the general property tax with the train of economic and political evils that follow it. The personal property tax is not only indefensible as an economic measure, but is a menace to public morality and sound government. Of the various substitutes for this form of tax, the habitation tax appears most worthy of examination and experiment. It roughly measures income, is difficult of evasion, equitable in incidence, and easy to administer. Whatever substitute is favored, some form of separation of state and local sources of income must be effected in order that the municipal system may obtain the necessary elasticity and flexibility.

Concerning the valuation of real estate, it is urged that this should be made by expert valuers, continuously in the service, and that tax officials should under no circumstance be elected by popular vote, but obtain their position either by appointment or under the merit system.

THE INCIDENCE OF TAXATION

By A. C. PLEYDELL

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If the people understood who really pays each of the various taxes, there would be great changes in our present tax systems. But there will not be complete reform until it is understood also who ought to pay the taxes. No discussion of the incidence of taxation can be profitable unless in addition to pointing out just who bears the burden of the tax we consider also who should bear the burden.

To show how taxes can be shifted, may result in popular attempts merely to unload burdens, unless it be shown also that unjust taxes injure every one, and not only those who actually pay them.

Technically the "incidence of taxation" refers to the final resting place of the tax, and "shifting" indicates the method by which the tax is passed on from the one who first pays it to the one who finally pays it. But the terms "incidence" and "shifting" are so often used interchangeably that for practical purposes we can speak entirely of "shifting" the tax.

A shifted tax means that the person who pays it to the government gets it back, through an increased charge, from some one to whom he sells or hires property or services. When the positive statement is made that a certain tax is shifted, it must be assumed that the law is enforced. Taxes that are not effective are not all shifted, even though they would be added to cost immediately were the law enforced.

Nearly all of our States have the general property tax, which in theory requires all property to be assessed and taxed at its real worth in money. But every one knows that such laws are not enforced, and the actual shifting of the tax upon any one kind of property is regulated by the degree of severity with which that property is sought for by the assessor.

Shifting is of various kinds and degrees. Some taxes do not increase prices by as much as the tax, because attempts to enforce the law are not made or are ineffective, and the tax is generally evaded. Some taxes increase prices by more than the tax because they restrict competition. Two kinds of taxes are not shifted: those levied upon a person as an individual or upon goods in his possession for use, and taxes on monopoly.

It is impossible in a brief paper to discuss the shifting of all kinds of taxes, with the modifications that result from the non-enforcement of law, or from the competition of other classes of goods or of persons less heavily taxed. But a few general principles and a few examples will cover the various classes of taxes.

With the increasing complexity of our social organization an increasing amount of taxes are paid to the collectors by persons who immediately add them to the price of goods or services. These taxes may, for convenience, be spoken of as shifted directly.

In this class are all the various taxes on manufacturing and business that add to fixed charges, and must be collected from customers or the manufacturer or merchant cannot continue in business.

Here we see the modifying effects of varying laws. Goods are sold in an open market, and the manufacturer whose machinery is heavily taxed has to sell in competition with those who are taxed lightly or not at all. He cannot, of course, add all his tax to the price of his goods. But the fact that he must add some of it keeps him from successful competition with the untaxed manufacturer, and tends to increase the price to the consumer, and to increase also the profits of the untaxed manufacturer. So the consumer pays the tax bill, indirectly, while the taxed industry languishes or moves to a more favorable State.

Taxes on the goods of merchants are similar in effect. The corner grocer must make a living, and the taxes on his merchandise must be paid by his customers. The man who can keep his taxes down will be able to undersell competitors and drive them out of business. If such taxes are strictly enforced in one town and not in another, the overtaxed man who raises

his prices drives away those of his customers who can deal elsewhere; and those who cannot will have to pay the tax through higher prices. They will have to pay also the increased cost of doing business on a small scale, for the merchant must shift it to them or go out of business; and they must put up with poorer service.

Decreased business means smaller rental value for the location. Thus excessive or arbitrary taxes on trade have an adverse effect on landowners, even if not exactly shifted to them.

Sometimes taxes are not shifted to the consumer because of ignorance. The business man who does not properly add his taxes to his prices will go out of business sooner or later, and wonder why he failed.

Mercantile licenses, though also paid by the consumer, have two advantages over the personal property assessment. They are effective, and thus prevent any advantage from evasion. If they are scaled according to receipts, they bear with practical equality on all merchants of the same class. Though they may be out of proportion to the respective rates of profits of a grocer and of a jeweler, still they treat all jewelers alike and all grocers alike. Of course, such taxes are also passed along to the consumer, and may bear with great inequality on various classes of purchasers.

Licenses at a fixed rate are more objectionable, and if at a high rate tend to establish a monopoly by limiting the number who have enough capital to pay the tax. This is seen particularly in the liquor taxes, which greatly increase the price of drinks and the profits of the liquor business.

The corporate form of conducting business is an improvement in commercial mechanism that decreases cost of production. Special taxes on competitive business corporations in excess of taxes on individuals or firms tend to check the use of this more efficient method of conducting business and add to the cost of using it. The burden falls partly on those who are enterprising enough to engage in this form of business, and partly on the consumer who pays a higher price because of the restraint on improvement in production.

Taxes on various forms of intangible property employed in commercial business, such as book credits and bank deposits,

add to expenses and are shifted to the customer. Taxes on such property when used otherwise are shifted to the borrower who is the consumer of the service done for him by the creditor. The shifting, however, is more indirect than is generally the case with taxes on goods.

The experience with mortgage taxation in New York illustrates how these taxes are shifted, and the principles are the same in the case of other forms of interest-bearing credits.

Prior to 1905 mortgages in New York were liable to personal property tax, though most of them escaped assessment. Therefore, though the few that were caught paid a tax of $1\frac{1}{2}$ to 3 per cent, according to locality, the interest rate was only slightly increased by the tax—about enough to cover the risk of being caught. Still, all borrowers paid this increased rate; a few lenders paid much more than the increase to the tax collector; and most lenders kept the added charge.

Then (in 1905) an effective tax was adopted, which the borrowers were forbidden to pay, and though the tax rate was only $\frac{1}{4}$ of 1 per cent in place of the higher personal property rate, interest rates rose at once, while loans declined. A year later a lighter recording tax was adopted, and interest rates fell, while loans increased—even though the borrower paid the tax and knew that he paid it.

Because taxes on certain forms of property, such as mortgages and money, are imperfectly collected, and therefore are not all added to the charge for loans, it is often asserted that the lender pays them. Every enforcement of such taxes has proved the contrary, by increasing the troubles as well as the expenses of borrowers, and reflection will show that it cannot be otherwise. The man who has the money expects a certain net return; if he cannot get it from one source, he will turn to another. Certainly, if another investment will yield him 3 per cent net, he will not accept 4 per cent interest on a mortgage and then pay 2 per cent tax. But the borrower needs the money, and he has to pay the market rate or go without. Suppose a 6 per cent tax were placed on all mortgages; would any sane man expect to borrow mortgage money at 5 per cent? How many people would leave their money on deposit for 3 per cent or 4 per cent if they were compelled to pay 5 per cent

tax on it? And with the money withdrawn from the loan market, how would the borrowers from the banks fare?

It has been said that taxes on capital could not be shifted if they were imposed uniformly and effectively on every sort of capital. Of course it is impracticable to secure such universal taxation. But suppose this could be done. Still capital would seek the best-paying investment as water seeks its level. The taxes on manufactured goods being paid by the consumers, capitalists would put their money into business directly and cut down mortgages or similar loans until interest or premiums rose sufficiently to cover the tax. No one has ever shown how a universal tax on capital could be adjusted so that no kind of capital could shift the tax — and when one kind did so shift the tax, other kinds would insist on getting the same net return.

The taxes on invested capital, as such, are many in kind, but all of them are shifted to the user, who in this case is the borrower, unless they are enacted during the term of a contract. If a State in which mortgages are exempt should suddenly tax them, all lenders who were caught would pay the tax until their mortgages were due. But this does not really affect the question, since argument on the shifting of taxes must assume the law to be stable as well as effective.

Bonds may seem an exception to the rule that the borrower pays the tax, as their holders are frequently assessed, and the interest rate apparently is not affected. But the bond is a mortgage with fixed interest, of which the principal value frequently fluctuates. Instead of demanding higher interest the buyer discounts the tax and pays less principal to the issuer, who, as a borrower, pays the tax through this reduction in the loan.

Here, again, lack of effective taxation creates confusion; the purchase of bonds by persons who escape assessment tends to keep up the price, so that the holder who gets caught has to pay more than his share.

Taxes levied directly on a person or on goods in possession for his consumption cannot be shifted. Such taxes are various, but all of them are vicious. A familiar one is the poll tax, that charges a man for being alive, and when he can't pay it,

often puts him in jail where he can't earn anything. He is not killed, even though he has not paid this tax for living, because his friends would then lose interest in him. Like a prisoner of war, he is held for ransom; and if he has no friends, the compassion of strangers is counted on to pay the tax and costs.

Another familiar tax is that on household goods or on clothing. Such taxes are really confiscation, for if a man has to pay \$10 a year tax on his furniture, he will soon have paid out the entire value in taxes, and never have made a dollar from the furniture with which to pay the tax. Thus he has paid for the furniture twice; in effect, the government has each year taken part of his furniture from him, and he has replaced it. And this is in addition to all the taxes on makers and sellers of furniture, which he paid in the purchase price of the furniture.

The inheritance tax is not shifted. When a person gets an inheritance, it becomes taxable property (usually), just as it was before it changed hands. But there is an additional tax because of the transfer of ownership; and the tax is really not on the property, but on the right to take for use property that has been given away because of the death of the former owner. The attempt to justify inheritance taxes as a charge for a privilege given by the State is an attack on private ownership of property. The right to inherit or bequeath is as essential to ownership as the right to buy or sell. Certainly the State is entitled to payment for services, but these are charged for in surrogates and other usual fees. However, as inheritance taxes are effective, and fall with fair equality as between individuals if properly levied, they are, if moderate, less burdensome than many other taxes.

A tax on incomes cannot be shifted, if levied regardless of occupation. If it applies only to some occupations, like a mercantile license or a professional tax, it will tend to be shifted through increased prices or earnings. If the tax rate is the same on all incomes, whether from earnings or business or investment, the tax burden will be heavier on workers than on investors.

The usual objection to income taxes is that they are inquisitorial. There is no doubt that an income tax is more fairly

proportioned to ability to pay than is the ordinary personal property assessment, since it does not fall upon unproductive personalty, and bears some relation to earning power of people or property. But an income tax does not fall at all in proportion to benefits.

It is often forgotten that when Adam Smith said taxes should be levied in proportion to ability to pay, he gave as the reason that ability was the best measure of the benefits received from government, which he deemed the real basis. Our assessing machinery does not fairly measure ability, and in our times better methods of measuring benefits than by ability have been worked out. These methods are the outcome of the principles of taxation laid down by Henry George, in accordance with Adam Smith's formulas. As a consequence it is coming to be understood that uniform assessment of all property is unjust because of the varying income-producing power and the greater variation in benefits received from government expenses.

One of the contributions of Henry George to this modern thought is his clear exposition of the exact relation between certain forms of public expenditures and the increase in site values of land. So immediate is this relation that it may perhaps indicate the line between those functions that are governmental in nature and those that are private. For instance, the maintenance of streets confers varied benefits, the value of which to each user cannot well be measured in money; yet each improvement in the highway is reflected in the increase of rents, which measure the worth of the improvement to the inhabitants. But in the case of a gas plant, the benefit to each user of gas is measurable. Though rents would rise if gas were supplied free out of the tax fund, the increase would bear no relation to the savings in gas bills to individual consumers. Such enterprises if municipalized should be run on a business basis, each consumer paying directly for what he gets.

Though this may seem a digression, it bears directly on the question, who should pay the taxes? If, on the one hand, it is just that the owners of ground values should pay for whatever governmental services enhance their holdings, on the other hand, it is unjust to tenants to raise rents artificially by furnishing services free which should be paid for by the users.

Taxes on monopoly cannot be shifted. But just in the degree that a monopoly is imperfect and open to competition, taxes on it tend to be shifted in proportion as the tax rises. To illustrate: A railroad is an incomplete monopoly; besides the possible construction of a competing line, there is usually some form of water or trolley competition; and there is always the marginal passenger or freight that does not need to travel, or will not if rates be too high. Rates may be all the present traffic will bear, but if taxes go above a certain point the rates must go up also, even though traffic will be reduced. The same principle applies to various other public service corporations. For instance, the amount of gas or electricity used depends on the price keeping down the use of oil or candles; and rates must be low enough also to induce a generous illumination. There is always a marginal consumer who can use less light or none. But a tax of \$1 a thousand feet on gas would force a rise in rates, however much the higher price reduced consumption.

To one form of public service corporation values, however, this principle does not apply. In so far as rates are higher than cost of service (including interest on construction), they represent the value of the privilege of using the highway, or the value of a private roadbed which is in effect a continuous parcel of land. Such a value is a ground value, and a tax on it cannot be shifted. The users of the service will not be affected by taxation of the corporation unless the tax more than absorbs this monopoly value. They pay the tax, but unless the government reduces rates they will pay that amount anyhow; but the corporation, if untaxed, will keep it.

There is only one perfect monopoly, the ownership of the site value of land. A tax on land value is not shifted, because the value of land is the relation of any piece of land to all other land. It is not a question of competing with some other form of utility. The value of land is at all times fixed by its desirability. No reduction of the tax will persuade or compel the owner to take less in rent nor will an increase in the tax enable him to obtain more. The value of a store site is determined by the business that can be done there, and the tax upon the site does not enter into consideration when negotiating for a lease. The value of a house site is determined by the competition of

those who desire it, and neither their ability nor willingness to hire it is affected by the amount of tax the owner pays.

The tax on buildings is another matter, for the production of buildings is a manufacture, and their cost is fixed by the same rules of supply and demand as govern other manufactured products. This difference in the character of land and buildings is often overlooked because they are taxed together as real estate.

While rental values have been used for illustration, the same principles of shifting apply to the price of land. The selling price of land is fixed by the net rental value. The gross rent is not changed by taxation, but the more gross rent is taken by taxes, the less will be the net rent and the smaller the price a purchaser will pay. It is unnecessary to elaborate on this point, but attention is called to it, because our taxes are nominally based on the selling price of land, when in reality that price is an untaxed value. The real basis of both sale price and tax is the rent any piece of land will command in the market.

A tax based on rentals of improved real estate and collected directly from the tenants is really an indirect tax on improvements because it falls on used property only. While it might help to relieve the owners of both used and unimproved land from some real estate taxes, it would somewhat reduce the rents received by the owners of used land for their improvements. But this reduction could not equal the addition to the tenant's expenses made by the tax.

The various classes of taxes that have been considered show wide divergence in their final effects. Some are shifted that should be shifted, and others that should not. And of those that cannot be shifted, some fall justly upon those people who should pay, while others are unfair and harmful. The fairness of a tax, therefore, cannot be judged by the mere fact of shifting or non-shifting.

Just taxation requires that payments for the support of government shall be in proportion to the benefits received or the special privileges enjoyed. There are at present many governmental activities whose benefit to individuals cannot be adequately measured, and many public expenditures that are not reflected fairly in ground values. Unless public expenses

are restricted to matters whose cost can be fairly distributed, there will be an excuse, even if not a necessity, for raising a good deal of revenue by special taxes. These should conform to the following rules:

1. Taxes should be so levied as to bear with equal weight upon all persons similarly situated.
2. Taxes should be so devised as to be cheaply and surely collected.
3. Taxes should not give any industry, by their incidence, an advantage over a competitive industry.
4. Taxes should fall on property, not persons, and upon visible property, not on the papers which show ownership of the property.
5. Privileges should be taxed in connection with the visible property through which they are exercised.

When taxes are effectively collected, the one who buys goods (or hires a service) pays through increased price every tax that has been laid anywhere along the line upon the materials in the goods or on the processes of making and bringing them to him — except where the tax was on a monopoly. Certainly if consumers are to be taxed in this indirect way, taxes should be so levied that consumers in the same class will pay the same tax.

The "general property" tax system does not shift taxes equally. Taxes are collected from the consumer that are not turned over to the government, while a few persons in the same class pay more taxes than they can collect under the stress of competition. To a large extent it prevents the final taxpayer from knowing that he is the one who pays the bills, and thus delays the adoption of a just system of taxation.

THE BASIS OF ASSESSMENT IN TAXATION

BY DEAN F. W. BLACKMAR

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EVERYBODY who has thought at all about the subject knows that the methods of assessment and taxation in the United States are irregular, unjust and inefficient. The evils of a dilapidated system have been felt by those who have suffered injustice, and have been pointed out by the wise ones for these many years. Legislatures have attempted to remedy the evil by adding one more patch to the crazy quilt of assessment and taxation. There is a growing feeling that the general property tax is entirely inadequate to meet the complex forms of modern property, and that some new system of taxation with new methods of assessment is very much needed. With the criticisms of the system appear scores of suggested remedies for the evil. These arise on account of local conditions, environment or previous conditions of servitude of the individual who has observed or felt the evil and desires to have it reformed.

If the evils are apparent the remedy is not so sure. What we need to-day instead of the perpetual harping on the evils of taxation is a program of action which will permanently and effectively remedy the evils. I take it that this Conference was called for the purpose of clearing away the rubbish of accumulated propositions of reform and reaching a consensus of opinion as to what would be good working plans for reform, or if this is impossible, there could at least be ascertained a working hypothesis for reform. The program must include a just, equitable and effective method of assessment. All of the difficulties of modern taxation center around the question of assessment.

Those who have attempted taxation reforms in legislatures have usually failed from lack of basic principles. All suggested reforms have been temporary expedients to lessen existing

evils. As a result, while they lessen the evil in one place they increase it in another. When our nation began its eventful course there was a small amount of property of a very simple nature. It was made up of land and chattels which were easily discovered and easily assessed. There has been a continued evolution of the forms of property until we have a hundred species where formerly there were but one or two. The government in its attempt to reach all forms of property has hastened to assess and tax each new form as it arose, frequently irrespective of the results of double, inequitable and discriminating taxes. This has brought about the direst confusion. There are three sources of the trouble; namely, a tax system that is unjust and inadequate, officials who have moved along the line of irregular political pressure, and the evasion and shifting of taxes by the citizens who pay.

It is idle under such circumstances to make a tirade against the tax dodger, for he is an economic evolution of the conditions we have permitted to grow up. It is idle to attack the assessors and officers for delinquency in duty, for they too are a product of economic and political conditions. It is useless to complain and scold at a dilapidation of a system, for it has been created piecemeal in an earnest endeavor to assess all property alike. The economic conditions of the country have entirely outgrown the system. A new program is needed involving the entire transformation of the tax system on basic principles. What property shall be assessed, how shall it be assessed, and on what basis shall it rest? These are the questions that concern us here in this Conference before we can reach any conclusions of what can be done.

We have made property the basis of taxation, and have tried to follow every form of property that arose. If we still hold to the property basis of assessment we are obliged to chase every form of property from a bicycle to a threshing machine and take a certain proportion of its estimated value. This is an imperfect process because it is difficult to determine its value. The owner does not know, the assessor does not know, the public does not know. Even when the article is supposed to be assessed at the full valuation it is difficult to determine the full value, but in most States in the Union articles are gen-

erally assessed at a certain per cent of the market valuation. This gives an opportunity for another variable, and as a result men with property of similar character may be assessed at a variance of 50 per cent. Granted that the assessors are honest and the people intend to pay their fair share of taxes, the assessment of property in the United States in most instances is a matter of systematic guessing. Of course, the earning power of property is also difficult to determine, but it would have the advantage of being a simple and universal basis, and, moreover, based on the capacity of the individual to pay the tax.

The true basis of assessment should be the capacity of the citizen to pay. This capacity should be determined by the earning power of property or else by actual income. The responsibility should be thrown more upon the person than upon the property, and he should be held to a strict responsibility. To make it more definite and to assess a constant tangible factor the actual income of property is the ideal basis of assessment, for this more nearly than any other method measures the capacity of an individual to pay.

While this is a difficult tax to assess and requires a refined and exact system of government, it may be accomplished if carefully adjusted. It will require a careful classification of taxpayers in regard to their occupation and of the property they hold. It will require also a classification of incomes in regard to amount. It will require the grouping of people in classes according to ability to pay. This may be difficult to attain, yet it follows the group system of economic competition which prevails to-day. It is in accord with the status of modern society. The progressive idea of taxation must of necessity be introduced. If people claim this is inequality, let it be granted that it is a species of inequality, but as Aristotle says, "Equality is for equals, and inequality for unequals." The whole economic system to-day is arranged in groups. The individual does not stand alone in his earning capacity or in his individual interests. The group system prevails everywhere, and the assessment of property and the collection of taxes should consider this group system.

Again, this basis of assessment applies to invisible as well as to visible salary; property tax appeals to that which is

evils. As a result, while they lessen the evil in one place they increase it in another. When our nation began its eventful course there was a small amount of property of a very simple nature. It was made up of land and chattels which were easily discovered and easily assessed. There has been a continued evolution of the forms of property until we have a hundred species where formerly there were but one or two. The government in its attempt to reach all forms of property has hastened to assess and tax each new form as it arose, frequently irrespective of the results of double, inequitable and discriminating taxes. This has brought about the direst confusion. There are three sources of the trouble; namely, a tax system that is unjust and inadequate, officials who have moved along the line of irregular political pressure, and the evasion and shifting of taxes by the citizens who pay.

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may take place they ought to be made on this universal principle.

Taxation on land values and taxation on the incomes of active business property are sufficient to cover all forms of property and to raise the revenue easily, equitably and without serious trouble. As it is universally known, New Zealand has adopted this method of assessment and thoroughly demonstrated its feasibility. There is no truer way to estimate the ability of the taxpayer. After fixing the economic rent or the normal income of land, let a tax be set upon the income. If land has an earning capacity of \$6, let the tax be on \$6, not on the \$100, which is the market value of land. And let this be on all lands irrespective of whether they are under cultivation or not. Hence, lands that are held for a rise in value because of the cultivation of adjacent lands by other people would pay their just share of taxes. After this divide all other economic activities into groups, such as first, *salary*; second, *agencies and professions*; third, *credit instruments*; fourth, *rentals of commercial buildings*; fifth, *rentals of dwellings* above certain values; sixth, *public service corporations*; seventh, *industrial corporations*; eighth, *merchandising*; ninth, *manufacturing plants*; and tenth, *lumbering, mining and extracting*. With a classification of this kind property would be so divided in the assessment that incomes would reach to a degree of accuracy beyond the conception of the most sanguine. It is not intended here to argue the pros and cons of income tax, but simply to say that there was no tax ever instituted whose good points were so thoroughly maligned and around which was thrown so much prejudice and injustice by those who oppose taxation as the income tax. It was too exact and too just to suit the artful tax dodger.

What is the value of a great packing plant? Is it the walls of masonry and the machinery within? No, it is the margin on the labor of a thousand men employed, coupled with the margin of hundreds of head of stock bought at a low price, transformed, and sold at a high price. There is no way under the sun to put your finger on the capacity that went to pay taxes except by making an estimate of its real earning power. What is the value of a smelting plant? In the walls and masonry

evils. As a result, while they lessen the evil in one place they increase it in another. When our nation began its eventful course there was a small amount of property of a very simple nature. It was made up of land and chattels which were easily discovered and easily assessed. There has been a continued evolution of the forms of property until we have a hundred species where formerly there were but one or two. The government in its attempt to reach all forms of property has hastened to assess and tax each new form as it arose, frequently irrespective of the results of double, inequitable and discriminating taxes. This has brought about the direst confusion. There are three sources of the trouble; namely, a tax system that is unjust and inadequate, officials who have moved along the line of irregular political pressure, and the evasion and shifting of taxes by the citizens who pay.

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quirements that a tax of this nature could not be put in practice. These, indeed, are obstacles which it would take a long time to overcome, but we can at least make this system a working hypothesis for all changes and gradually grow toward the ideal. It is assumed that a tax of this kind should be universal in all of the States to make it successful, and that the federal system is in the way of uniform taxation. For that matter it is difficult to establish any sort of uniform and universal reform on account of the diversity of state laws and constitutions. Yet such things have been accomplished. If this association does the work expected of it, the unification of sentiment, law and system will be greatly advanced. Moreover, if all the new tax laws should work toward this end, a gradual change for the better would take place. To accomplish anything in the way of reform there must be an ideal to work toward, a program to follow.

Suppose as a beginning the land and the improvements should be separated in taxation, it would be a step in the right direction. Suppose state and local taxation should be separated, and the revenue from public service corporations should be devoted to the expenditures of the State, then the State could consider the corporation as a whole and tax on the earnings or the income. Suppose all household furniture not used in a commercial sense should be exempt, it would be a start toward breaking up a clumsy general property system. These and other movements would hasten us on toward a system we must finally adopt before the tax question is permanently settled.

In the assessment of property the smallest territorial unit should be the county, or possibly the municipality in very large cities. The local assessment should be entirely separated from state assessment. The revenue from local assessment should be applied to local expenditures, and the amount raised from state taxation devoted to state expenditures. These state revenues should be derived from general corporations, such as railroads, telephones, telegraphs, express companies, insurance companies, etc. These would furnish sufficient revenue for state expenditure. In case of any pro rata it could be redistributed to the counties.

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BUSINESS AND PROFESSIONAL TAXES AS SOURCES OF LOCAL REVENUE

By H. A. MILLIS

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IN 1902 upwards of 82 per cent of the tax revenues of our state and local governments were drawn from the general property tax. And 7.24 per cent were drawn from special property and business taxes, a part of which are closely related to the general property tax.

This situation is not satisfactory. In the first place, the rates imposed have increased until they have become burdensome. This is due largely to the concentration of population in cities, giving rise to rapidly increasing expenditures resting upon taxation. In many of our cities, the combined rates for state, county and municipal purposes would exceed one and one half per cent on a full valuation of the property assessed.

In the second place, partly as a result of these high rates, the general property tax has broken down in its administration. Evasion and undervaluation are very generally practiced, where possible. Only a small fraction of moneys and credits are listed. In the assessment of merchants' stocks, the proprietors take advantage of the ignorance of the assessor and of loopholes in the law, and great undervaluation results. Manufacturers' stocks are not assessed according to law. And so it is with most forms of personal property other than the live stock and implements of the farmer. In some instances, it is true, a better administration has brought about an improvement as regards values returned; but nowhere has even the best administration succeeded in carrying out the intent of the law. Because of the administrative difficulties met with, many have concluded that it is better to change the law and to get at taxable ability otherwise than through the most inclusive property tax. There is a demand that at least certain forms of personal property be relieved from *ad valorem* taxation.

In the third place, there is, at the same time, a demand that direct taxation shall be extended. Property holdings now taxed are not sufficiently indicative of ability to contribute to the support of government. There are many professions and trades yielding large returns to those who follow them, scarcely touched by property taxes. In some lines of business little tangible property is used, while where there is considerable property used, it must be admitted that as between different kinds of business there is no relation between the amount of such property and the amount of profit reaped. Hence to reach all ability directly and equitably it is necessary to employ more than mere property taxes uniformly levied.

Of the measures to equalize taxation and to keep down the general property tax rates, the income tax is most frequently urged. Such a tax has been widely employed in this country as a source of state revenue and not infrequently of local revenue as well. What has our experience with income taxation been?

We have used both "faculty taxes" and "income taxes" in the narrower sense of the term.

"Faculty taxes" were employed at some time or other in all save two — Georgia and North Carolina — of the thirteen States in existence at the time of the formation of the Constitution and, for a time, in the Northwest Territory. These were supplementary to taxes on property and polls, where the latter were levied. The incomes of professional men, of skilled mechanics, occasionally of less skilled workmen, sometimes those from the dealing trades, and occasionally those from toll bridges, ferries and the like, were listed and taxed along with property. Property was, as a rule, assessed according to its annual value or else listed and taxed at rates, specified in the law, based upon that value. To reach income from various sources directly seems to have been the working ideal.

But because of poor administration and the narrow application of the law, "faculty" counted for little in the returns. In most instances it was dropped from the taxable list before the close of the eighteenth century and in the other States, save Massachusetts, it disappeared with the adoption of the general property tax in its modern form.

Though there is a question as to what constitutes an "income

tax," if we follow Professor Kinsman's account,¹ income taxes, properly speaking, have been employed in sixteen of the commonwealths. They are still employed in five States—Massachusetts, Virginia, North Carolina, South Carolina and Tennessee.

The sixteen embrace Massachusetts, Pennsylvania, Delaware, and all of the Southern States save Arkansas and Mississippi. The income tax has also been employed as a source of local revenue, as in Louisiana and Georgia.

In Massachusetts the income tax developed from the "faculty tax" already mentioned. In six States it was adopted during the 1840's, when the treasuries were in straitened circumstances because of unremunerative improvement and banking enterprises undertaken. In five more it had its origin in the Civil War. In at least two of the other four States, the income taxes were introduced under somewhat similar circumstances. It was necessary to find new sources of revenue in order to keep the general property tax rates within due limits.

But while largely the invention of necessity, these taxes have usually been supplementary to the property taxes used. In Virginia, North Carolina, Alabama and South Carolina alone have they, for any considerable period, been sufficiently inclusive to be called general income taxes, and in North Carolina since 1868 incomes from property taxed have not been assessable under the income tax law. Like the "faculty taxes" they have generally been devised to reach special sources of income not otherwise reached.

From the point of view of revenue produced the income taxes have been of little importance and, where retained, have become almost a farce. This small yield is partly explained by the special character of the taxes imposed. It is partly explained by careless administration or failure to enforce the law. And this failure to enforce the law has been due, to an extent, to the fact that the taxes have frequently been regarded as class taxes, but more to the fact that their administration has been incidental to the work of local officials while the revenue was to be paid over to the state treasuries. And finally, where an honest effort has been made to enforce the law, the opportunities for evasion have proven too difficult to overcome.

¹ In publications, American Economic Association, Third Series, Vol. IV.

The state income taxes have been little better than failures in practice, and slight improvement can be expected so long as we rely upon the personal declarations of taxpayers in making assessments. Our experience with federal and state income taxes lends no hope that under ordinary circumstances can an income tax be made satisfactory unless by getting at the greater part of incomes before they come into the hands of the individuals who bear the tax burden. But unfortunately, in state and local income assessment, especially if the taxes are supplementary to property and corporation taxes, this cannot be done to any great extent. State and local income taxes are not at present practicable measures.

But is there not an alternative? Can we not make use of business and occupation taxes so levied as to reach incomes with a fair degree of justice and thus supplement property taxes so as to prevent these from becoming unduly burdensome, so as to make it more feasible to give up the taxation of property where it proves difficult, and so as to reach directly ability not directly and adequately reached by such property taxes as can be employed with a fair degree of success? Such taxes have occasionally been recommended for adoption for local purposes, and have rather frequently been pointed to as possibilities worthy of consideration and possibly of adoption where not now used. Our experience with such taxes, usually denominated "business license," "privilege" or "occupation taxes," has been extensive. What has this experience been and what does it teach?

The history of these business taxes cannot be given here. Suffice it to say that in several instances those levied primarily for revenue have long been used. In California, Texas and Louisiana their use antedates annexation of the territory. In Virginia they were used as early as the middle of the seventeenth century. In some States, as in Ohio and Michigan, they were widely employed under rather primitive conditions, but given up as property taxes became more inclusive and the general property tax was finally introduced. But in the majority of instances, extensive systems of business and professional license taxes for revenue as opposed to regulative purposes were introduced like the income taxes, when the treas-

uries were depleted during the 1840's, 1850's and the Civil War period. Frequently they and the income taxes were complementary. Extensive use by cities usually accompanied or preceded such use by the States.

Once introduced they have usually been retained. In California, it is true, they were abolished for state purposes some thirty-five years ago, and have since been systematically employed by only a part of the cities. In Texas, in so far as they rested on "useful occupations," they were abolished by the last general assembly and are no longer to be employed by the state, county and municipal authorities. In a few instances the systems have been materially contracted. But in most of the Southern States, — where they are chiefly employed, — if due allowance is made for readjustments after the close of the Civil War, they have not only held their own, but have been imposed upon more and more occupations, at generally increasing rates, for both state and local purposes.

At present nearly all of the commonwealths levy license taxes on dealers in liquors, peddlers and traveling venders, and various kinds of amusements, primarily for the purpose of regulation or suppression. Those imposed upon the liquor traffic are usually very productive. Again, in most of the States taxes are levied on the business of insurance companies, and in not a few instances the taxes on railroads, express, telegraph, telephone and car companies take the form of a levy upon their gross earnings, either in lieu of or in addition to taxes on their property. But with these we shall not deal. The discussion will be limited to those taxes falling upon many occupations and trades and levied primarily for the purpose of revenue. Such are now rather extensively employed in about one third of the States, the object being to keep the general property tax rate down, to replace or to supplement property taxes, and to reach income not reached through such property taxes as are employed.

These taxes are more or less systematically employed for *state* purposes in Pennsylvania, in Delaware, and in all of the Southern States save South Carolina, Missouri, Arkansas and Texas, and also in New Mexico, Idaho and Montana. In practically all of these States and in several others similar taxes

are employed — and frequently much more extensively — for municipal purposes. In some cases (as in North Carolina, Florida, Alabama and Louisiana) the county governments are permitted to use — with minor exceptions — the business taxes employed by the State, but in other cases (as in Virginia, Georgia and Kentucky) they may not be so employed, the county governments being practically limited to the general property tax.

Thus, business and professional license taxes, levied for the revenue which may be derived from them, are extensively employed, especially in the South, and are generally imposed by both State and municipality, and not infrequently by the county as well. What form do these taxes take? How have they worked? What as to their availability, especially when applied to the mercantile trades, manufactures and the professions?

The legislation bearing upon these taxes comprises a great mass of details not capable of accurate generalization. There is little which may be regarded as typical. At the one extreme we find a few occupations and trades taxed for revenue purposes; at the other, practically all trades and businesses carried on in cities. In Louisiana we find the most inclusive system for state purposes. There the constitution of 1898 (Article 229) authorizes the general assembly to levy license taxes upon "all persons, associations of persons and corporations pursuing any trade, profession and calling, except clerks, laborers, clergymen, school-teachers, those engaged in mechanical, agricultural, horticultural, and mining pursuits, and manufacturers other than those of distilled, alcoholic or malt liquors, tobacco, cigars and cotton-seed oil." The State makes full use of the power thus given, and authorizes the municipalities and parishes to levy upon the same subjects provided that with the exception of the liquor licenses the state rates shall not be exceeded. In many of the cities in other States systems still more inclusive are found. Wilmington, N.C., for example, some years ago levied license taxes upon 124 classes of business. The license tax ordinance now in effect in Atlanta contains 466 items, thus permitting few persons other than manual laborers to follow their callings untaxed.

The exemption of most branches of manufactures from license taxation is, however, very general in the South, and where this

exemption does not obtain the business tax is almost nominal and is added to a property tax.

The mercantile trades, on the other hand, are very generally taxed — not only those with little stock in trade, but also those with regular stocks of goods and fixed places of business. In a few instances, as in Pennsylvania and Virginia, the license taxes are in lieu of taxes on the stocks of goods carried, but this substitution is rather exceptional. More frequently they are a second contribution exacted, being imposed because of fiscal necessity or because of the feeling that such property would otherwise not bear a fair share of the tax burden.

The professions are very generally, though by no means universally, taxed as a part of the license tax systems employed.

The revenue from the business tax systems now employed varies greatly of course with the number of subjects embraced within them, and especially as taxes are or are not imposed upon those engaged in wholesale and retail trade. Several States and many cities are deriving a fairly certain and large revenue from business licenses, thus materially lessening the general property tax rates.

In Louisiana licenses other than for the liquor traffic in 1902 produced one eighth (12.49 per cent) as much revenue as the property taxes levied for state and local purposes. Virginia in 1902 derived 8.25 per cent as much revenue from licenses other than the liquor traffic as from the general property tax. Richmond in 1904-1905 derived 14 per cent as much. The percentage for other Southern cities for 1899 were: Atlanta, 15.5; Charleston, S.C., 18.6; Savannah, 21.2; Augusta, 26; Mobile, 57.3.

It should be pointed out, however, that most of the license tax revenue is invariably drawn from the liquor traffic and the ordinary mercantile trades. The great majority of the subjects taxed yield little, and this is especially true of the liberal professions. The explanation of this is found partly in the low rates imposed, and partly in the fact that there is less business not now reached to some extent by property taxes than is sometimes supposed. Nevertheless, the revenue is distinctly worth the while.

Turning from fiscal results let us briefly note some of the shortcomings of the system as found especially in the Southern States.

In the first place, there has been much complaint of evasion. In spite of the license required evasion practiced by the members of the liberal professions has been very flagrant. Again, it is a rather common occurrence, especially in trade, to make one license serve where two or more are required for the businesses combined. But evasion of this kind is not inherent in the business license tax system; it is due to inefficient administration. If the taxes were heavy enough to make collection worth the while, inspectors might be appointed, as they have been for some years in Atlanta, and the law fairly well enforced. However, most of the evasion has taken another form to be indicated a little later in the discussion.

Again, the complaint is frequently met with that these taxes are inconvenient and that they repress and fetter industry. That they are inconvenient, especially in the small trades where frequent changes are made requiring repayment or transfer of the license, is true. That they do repress industry must be admitted, but that is characteristic of most taxes. If the system were arranged so as to be just and stable, the business license system would not be particularly objectionable on this score. Of vastly more importance is the fact that the system involves special legislation, is necessarily arbitrary, is made reasonably just only with difficulty, and has everywhere been subject to almost constant change with its uncertainty and loss of efficiency in administration.

The license tax systems as they exist in the Southern States and cities are the result of almost constant tinkering on the part of the legislative bodies. There and elsewhere the frequency of amendment is the thing most striking to the investigator. This fact is due to the many problems which have arisen in connection with such taxation. Among these problems have been: what subjects shall be taxed; what weight shall be given to such taxes as against property taxes; what rates shall be imposed upon the several subjects thus taxed so as to make the contributions exacted relatively fair; what exemptions shall be accorded, and how shall payments be graduated so as to make them fair within each trade taxed.

Where the system has not been very inclusive, struggles have been frequent over what things should be embraced within it.

In nearly all of the Southern States and cities there has been a fairly constant struggle between the owners of real estate and those interested in licensed business over the relative amounts of their contributions. The problem of what is a fair division of the burden between property and business has not been and perhaps cannot be satisfactorily and definitely settled.

Again, there has been much legislation designed to make rates fair as between taxable trades, with its incidental struggles and shifting of burdens. To illustrate, in Louisiana, since 1880, those who follow most trades have been divided into classes based on gross receipts or sales and charged with specific sums according to class. The approximate percentage of receipts taken during this period has remained fixed for retail merchants alone. In 1882 the rates on wholesale merchants were doubled. In 1880 manufacturers (in so far as they were taxed in this manner) were taxed at about $\frac{7}{10}$ of 1 per cent of their gross receipts; in 1902 those not specifically provided for at $\frac{1}{10}$ of 1 per cent. But the rate on the receipts of refiners of sugar had been changed to $\frac{1}{4}$ of 1 per cent; on saw mills, distillers, brewers, and certain other manufacturers to $\frac{1}{4}$ of 1 per cent. In 1880 gas, water and telephone companies, like manufacturers, were taxed on their gross receipts at $\frac{1}{10}$ of 1 per cent; in 1902, at $\frac{7}{10}$ of 1 per cent. In 1880 professional men were taxed at about $\frac{1}{2}$ of 1 per cent of their gross incomes; in 1903, at from $\frac{2}{10}$ of 1 to 1 per cent, the taxes being generally regressive. Thus had the burden been redistributed among these classes. Elsewhere changes of the same kind have been of frequent occurrence.

It may be urged, however, that such changes with their incidental struggles have been due in part to a lack of system and to a failure to adopt rates generally recognized as fair as between interested classes. Had the rates been imposed with reference to the net income expected, and with reference to the possibilities of shifting, much of this tinkering would have been avoided. But it must be admitted that as things go in these matters, the rates as they stand at any time will be more or less arbitrary, will be considered unfair as between trades, and this will incite change.

Another problem more difficult, and not as yet solved by

our States and cities, relates to the graduation of rates so as to be fair among those following a given trade or profession. In the Southern States, except Louisiana, most of the taxes are uniform upon all the members of the given trade. But where there is much difference in the amount of business done the uniform impositions become very unfair and, if large enough to yield a revenue worth the while, become a distinct evil.

This was the situation in Louisiana prior to 1880, when the essentials of the present methods of graduation were introduced. Under the tax law of 1879, the State, in order to get an adequate revenue, imposed very heavy license taxes and almost all without graduation. To these, local impositions, frequently much heavier, were added. The burden imposed upon those whose net earnings were least and the injustice of the system gave rise to a struggle in the constitutional convention of 1879 to eliminate all privilege taxes save those required for regulative purposes. However, the use of purely revenue privilege taxes was retained, the provisos being made that the local governments should not impose amounts in excess of the state rate upon any subject save the liquor traffic, and that all such taxes, whether used for state or for local purposes, should be graduated.

Since the adoption of the constitution of 1879, hotels, boarding-houses and lodging-houses have been taxed roughly according to the number of rentable rooms. This is a definite and not particularly unjust graduation of the payments required. Theater buildings and the like have been taxed according to seating capacity — an equally satisfactory arrangement. Such branches of manufactures as were formerly licensed in New Orleans were taxed according to the number of employees, and this principle of graduation has been applied elsewhere. It is definite, easily applied and comparatively fair. But some other method must be found for graduating the exactions made of professional men, wholesale and retail dealers, and of financial institutions. In those cases great difficulty has been met with in finding a principle of graduation which can be easily and successfully applied, and which is at the same time equitable.

In Louisiana the graduation in the vast majority of trades and the professions has been on the basis of gross earnings, and

this, or the related one of purchases, has usually been applied elsewhere to the mercantile trades when uniform taxes were departed from. It has, of course, been frequently applied to corporations and with great administrative success. But because of the absence of safeguards in the taxation of merchants and other trades, it has been accompanied invariably by a vast amount of evasion and dishonesty. In Texas merchants generally rated themselves in the lowest of the eleven classes; in Pennsylvania and Virginia, where merchants' stocks are exempted from taxation, there has been much dereliction of duty on the part of the officials charged with the enforcement of the law, or else much perjury practiced by the merchants. And in Louisiana the same evil is widespread. A few years ago of the 1603 saloons licensed in New Orleans, there were only nineteen which reported gross receipts in excess of \$5000 per year, and many of those reporting less than \$5000 were known to spend more than that amount for wages and rent. In other lines of business there is less dishonesty and perjury, but much is admitted to exist. In spite of the fact that the authorities may question returns made, and have books and accounts and other evidence produced in the courts, and in spite of penalties for false returns, the system is rotten throughout. Unless there is to be much publicity and inspection of books and accounts — and these are objectionable and not very effective — the business tax thus graded is little better than the self-assessed income tax. It were better to tax professional men uniformly. In the taxation of merchants it is doubtful if it is any improvement over taxation of their stocks.

But is there no basis for graduation which will prove more acceptable? Is there no basis which will be perfectly definite, easily measured, will render evasion difficult or impossible, and which will at the same time be reasonably just?

There is. In 1904 the legislative body of the Province of Ontario, in an *act respecting municipal taxation*, adopted the assessed value of the real estate occupied in business and in the professions as the basis for their "business assessment" and taxation. (See Statutes of Ontario, 1904, Ch. 23, Sec. 10, and same, 1906, Ch. 36.) Under this law almost every trade, business and profession conducted in a municipality is made

taxable for municipal purposes on some percentage of the value of real estate occupied at the rate imposed on taxable real estate and incomes.¹ The percentages of the assessed values of real estate occupied taken for the "business assessment" vary from 25 in several trades to 150 in the case of distillers. Only incomes from sources other than property and businesses taxed are taxable under the income tax law. Personal property is exempt.

What promise does this system hold forth?

The base for the imposition of the tax is definite and its amount is easily ascertained. No inquisitorial methods need be employed; there is little opportunity for evasion and dishonesty. It may be applied to all professions, trades and business with a definite location. If it is applied, one assessment will suffice in most cases for real estate and business taxes, thus simplifying and reducing the expense of administration.

But is it fair as between those engaged in a given business or profession — say retail trade? It must be admitted that the value of real estate occupied is not an accurate index of net receipts from the business done. It is not so accurate as gross earnings, if these can be accurately ascertained. But in practice in such a country as ours, with our habits of tax evasion and our dislike for inquisitorial methods, it is far preferable to taxation according to gross earnings except in the case of public service corporations. The Ontario system promises to be vastly superior to any system of business license taxes we have had in the United States. It is not ideal by any means. It is not equitable as between taxpayers of a given trade. Necessarily it involves special legislation, and the selection of percentages for the several trades is, and must be, more or less arbitrary. But it is not grossly unfair, and any system of taxation must be more or less arbitrary. Moreover, it eliminates most opportunities for evasion and dishonesty and at the same time is simple and inexpensive in administration.

The business license tax systems in the Southern States are

¹ It is worth noting that Professor Ely in the *Maryland Tax Commission Papers*, 1888, pp. 187-188, recommended the taxation of stores, offices and manufacturing establishments, on their rental values and the exemption of stocks, furniture, etc.

firmly established. Though many would advocate their abolition and heavier taxation of property or the substitution of an income tax (for state purposes), it is noteworthy that not one of the half dozen special tax commissions in the commonwealths employing those taxes has recommended such action. These tax commissions have recommended their retention, and in this have found support in public opinion, in spite of their arbitrariness, constant change, injustice and evasion, because of the relief they have afforded through the lower property tax rates, and because they are believed to reach ability not adequately reached in other ways. Were some such system as that of Ontario substituted for those now employed, it is altogether probable that business taxation would find greater favor than it has in the past.

One point remains to be discussed, viz. the incidence of business and professional taxes.

It is generally assumed by tax commissions and public officials that these taxes are shifted by the taxpayer to the consumer of his product or services. But that this is not always true is certain. The taxes on the professions are usually so small that they do not affect the customary charges for services performed and therefore are not shifted. The same thing is true of many other subjects in the business tax list. When imposed upon manufacturers, the incidence is in doubt. The shifting will depend among other things on the generality of the tax with reference to the market supplied, its amount, the prospect of its continuance, and the form it takes. Taxes imposed on wholesale and retail dealers will ordinarily be shifted to the consumers, though this may not take place to the full extent of the sums imposed.

Or, to put the matter in a different way, the incidence of these taxes is uncertain. This uncertainty is one objectionable feature of the system. Taxes seemingly equal may impose upon taxpayers very different burdens. Hence if the system is employed, the rates imposed must be fixed with reference to the possibilities of the burdens being shifted in varying degrees.

These are the more important considerations connected with business and professional taxes. They may be used as a substitute for taxes upon certain forms of personal property which

do not work well in practice; they may be used as a substitute for the income tax which is impracticable as a source of state and local revenue, to reach income not directly reached through property taxes; they may be used to keep down the property tax rates. Nevertheless, it must be recognized that there are difficulties inherent in the system. It is more or less arbitrary and unjust, and this injustice may be increased by the uncertainties of shifting. If it is to be employed, the levy must be based upon a tangible fact, and this is found in the Ontario system.

MR. RUTHERFORD: I shall take great pleasure in introducing to you Governor Coe I. Crawford, of South Dakota. It is impossible for Governor Crawford to be with us this afternoon, and I am sure we shall all be pleased to hear a few words from the Governor of the State of South Dakota. (*Applause.*)

GOVERNOR CRAWFORD:

Mr. Chairman, Ladies and Gentlemen:

I assure you that I am not going to take very much of your time, when I know you are all anxious to go out to be photographed. I arrived only yesterday, and with great interest listened to a part of the program at the evening session, and to that part which it has been my privilege to hear this morning. I discover that there are two classes here; there are those who, as professors in the schools and as close special students of the entire subject of taxation, are presenting wonderfully interesting views of the whole question for your consideration. There are also those who apparently come from the field, the great field of active life and official service, where these different, imperfect systems of taxation are being tried and applied. Of course to these two classes, these workers from the field and these special students, there is one goal which both alike are seeking, and that is, some solution, or something in the nature of a solution, or some step toward the solution, of these great questions of taxation which will be practical help to all.

It is an ancient maxim or principle which is deeply embedded in Anglo-Saxon forms of government, that these principles of taxation, in order to be put into effect, must be adopted by the people, and whether it be in the great Empire State, in New York City, or in the great open spaces of South Dakota and North Dakota, or out in Utah, the measures that are determined upon as good, before they can be practically good, must be recognized and endorsed by the people of those respective communities and commonwealths. The people hold the power in their hands, and whatever is proposed must be something which, when submitted to them, will meet with the approval

of a majority. That must be borne in mind all the time, because that is the great jury that must pass upon all theories, that must pass on every proposition before it can be crystalized into statute and made effective.

Now, out in our State, which is only one portion of this great field, we have a constitution. We have different forms of property, we have revenues that we must raise, and we have environments with which we must deal, out on the wide prairies, with a constituency a little like the professor from Texas told us about. Over in New York, where an acre is worth a million or ten millions, and where life is stifling in its congested environment, there is an entirely different situation.

We have a local assessor elected by the people in his township or village, or in the municipality; he is elected by those people to assess their property. It is a local institution there, a local custom, that he shall assess their property; and if you would undertake to change that, and have some one appointed from some source above these people and to adopt the principle of valuation upon which revenue is to be raised, you will have to deal with these people, because it comes right home to them. We have the state board assess one class of property, public service corporations, express, telegraph and railway companies, and make a valuation upon their property. We have got to deal with the local communities. I think myself that the time has come when we must recognize that there is real and personal property, and then there is another class of property—the moneys and credits and all sorts of things. If you are going to exempt these things and let them get off scot-free, placing your assessment on something else, you will have to deal with the people who pay these taxes and bear these burdens. While in New York City it may be a question that is working out in the direction of a single tax, out where the great majority of the people are farm owners, as with us, you will find that they would not take very kindly to the exemption of this intangible property and the placing of the burden upon them; but it is certainly a step in the right direction to have all these questions placed in the crucible for analysis, and to bring the professor from his chair and place him alongside the man who comes from the field of active life and experience, that they may exchange views and

discuss with each other these great problems. I am glad to see you all getting so near together, and I congratulate you upon what is being done. I regret that I cannot stay through the session. I want to say that I believe a permanent organization, constantly pounding away at these questions, is something that is not only necessary, but that I believe will result in time in effective legislation that will be helpful and that will equalize these burdens. (*Applause.*)

SEVENTH SESSION

THURSDAY AFTERNOON, NOVEMBER 14, 1907, 2 TO 5 O'CLOCK

CHAIRMAN, GOVERNOR GUILD OF MASSACHUSETTS

PROGRAM

1. TAX PROBLEMS IN MAINE. — IN VIEW OF ADAM SMITH'S FIRST PRINCIPLE OF TAXATION.
Professor Robert J. Sprague, Department of Economics and Sociology, University of Maine, Orono, Me.
2. GENERAL PROPERTY TAX AS A SOURCE OF STATE REVENUE.
Professor J. H. T. McPherson, Professor of History and Political Science, University of Georgia, Athens, Ga.
3. SEPARATION OF STATE AND LOCAL REVENUES.
Professor Edwin R. A. Seligman, Columbia University, New York, N.Y.
4. SEPARATION OF STATE AND LOCAL REVENUES AS A PROGRAM OF TAX REFORM.
Professor T. S. Adams, Wisconsin University, Madison, Wis.
5. A NEW METHOD OF RAISING STATE REVENUE.
C. B. Kegley, Master State Grange, Pullman, Wash.
6. TAXATION BY THE STATE OF PENNSYLVANIA.
Professor Joseph A. Beck, Department of Economics, Western University of Pennsylvania, Pittsburg, Pa.
7. TAXATION; THE UNIT RULE OF ASSESSMENT; A HOPE FOR THE FUTURE.
William O. Matthews, Attorney of Ohio Tax League, Cleveland, Ohio.
8. DISCUSSION.

TAX PROBLEMS IN MAINE.—IN VIEW OF ADAM SMITH'S FIRST PRINCIPLE OF TAXATION

BY PROFESSOR ROBERT J. SPRAGUE

Department of Economics and Sociology, University of Maine,
Orono, Me.

ADAM SMITH's first principle was:

"The subjects of every State ought to contribute to the support of the government, as nearly as possible in proportion to their respective abilities; that is, in proportion to the revenue they respectively enjoy, under the protection of the State. In the observation of neglect of this maxim consists what is called the equality or inequality of taxation."

This proposition has been criticised and defended for over a century, but it still stands as the clearest general statement of the goal toward which all the leading European countries are tending. France, Germany, Switzerland, Netherlands and England, with their multiple taxes and progressive systems, are working toward the realization of the great Scotchman's first principle. The system of taxation enforced by any commonwealth should be modified to meet the peculiar condition of resources, location and traditions of the population. So I shall not attempt to generalize for all of America, but shall confine my time to the problems of the Pine Tree State.

I propose first to examine the actual conditions of taxation in a selected Maine town; secondly, to discuss briefly the peculiar and immediate tax problems in Maine; and thirdly, to outline a few possible reforms of the system.

This will be done with the intention of exhibiting to what extent Adam Smith's principle is realized in Maine.

The selected town which I shall examine, I have studied on and off for a year, and am personally acquainted with a large proportion of the people and their economic conditions.

The town has a population of 3257, probably three quarters of them living in the village. The property is, as a whole, assessed at about 70 per cent of its actual value, and the rate

of taxation is $2\frac{1}{10}$ per cent. The town has four pretty well defined classes of citizens,—the farmers, the mill and factory people, the tradesmen, and the professional class, which includes the faculty of a college.

A selected typical farmer of the poorer class yields the following facts:

Forty-nine acres of land, with buildings, assessed at . .	\$900
Personal property	<u>140</u>
Total property	\$1040
Property tax	\$29.12
Poll tax	<u>3.00</u>
Total tax	\$32.12

After long and careful consideration, the farmer told me his income could not exceed \$400. The rental value of the house should be added to this, making \$475, after repairs to buildings and upkeep of the place were provided for. He regarded his farm as much underestimated by the assessors, and would not think of selling for twice the assessment. So from the total income of products and rent, \$475, we must deduct at least \$100 for interest on money invested, leaving \$375 as the net income of the plant on which he gets his living.

Now for the privilege of earning \$375 on a farm under the protection of the State, he pays \$32.12, or $8\frac{1}{2}$ per cent of his income.

Let us now glance at a typical farm of a higher grade. This farm contains $47\frac{1}{2}$ acres, with buildings, assessed at . .	\$2730
Personal property assessed at	<u>380</u>
Total property	\$3110
Property tax	\$87.08
Poll tax	<u>3.00</u>
Total tax	\$90.08

After several days of careful computing, the farmer gave the following estimates of his situation:

Total income, after providing for repairs to farm and buildings, including rental value of the house	\$1100
Interest on market value of plant	<u>300</u>
Net income including rent	\$800

For the privilege of enjoying this income under the protection of the State, he pays \$90.08, or $11\frac{1}{4}$ per cent on his net income.

In this case the tax of \$90.08 is the lowest tax ever paid on the property. The owner said that he had paid as high as \$176 on the same plant.

Of course there are developed attractive features in farm life, such as health, citizenship and independence, but, after all, a highly unfair per cent of the net income is taken for taxes.

These are closely studied cases which, as far as I can learn, are typical of the general condition of the farmers in the Penobscot Valley. A great many more cases might be given only leading to the same conclusions.

Let us now examine the contribution made by the wage-earning class of citizens for the support of the local government. In one of the largest manufacturing plants of the town I obtained the incomes of all the regular workmen, excepting the superintendents. The list includes only those men who work the year round for this corporation, and who have no other considerable income.

The incomes are as follows:

7 men at \$1040.00 per year	. . . . .	\$7280.00
3 men at 832.00 per year	. . . . .	2496.00
2 men at 780.00 per year	. . . . .	1560.00
3 men at 728.00 per year	. . . . .	2184.00
8 men at 624.00 per year	. . . . .	4992.00
8 men at 557.44 per year	. . . . .	4459.52
19 men at 514.80 per year	. . . . .	9781.20
5 men at 507.00 per year	. . . . .	2535.00
55 men,	total income,	\$35,287.72

These men pay taxes as follows:

32 men, poll taxes at \$3	\$96.00
All others pay an aggregate of	316.70

The total tax is $1\frac{1}{4}$ per cent of the total income.

Thirty-seven men paying only a poll tax, or none at all, have an aggregate income of \$24,724.88, and pay \$96 to the government, or $\frac{1}{25}$ of 1 per cent of their income.

The question of taxes paid indirectly, by this and other classes, as rent to the landlord, will be considered later.

Let us now consider the case of the professional men. During the year 1906-1907, the college paid for instruction and administration to persons living in the town, a total of \$86,075. This does not include wages paid to janitors and helpers of various kinds.

Out of this group of men 11 pay an aggregate tax of	\$618.90
10 men pay	58.00
and 30 men pay	90.00
The whole group pays	<u>\$766.90</u>

directly for the support of the local government, or $\frac{1}{10}$ of 1 per cent of the aggregate income. Eleven men of this group own their residences, and if the taxes paid by them were subtracted from the total taxes, and their incomes subtracted from the aggregate incomes, the remaining instructors would be found to pay only a small fractional part of 1 per cent on their incomes. Some of these people have incomes from other sources, but no account is here taken of such.

The three leading and well-established physicians in the town have an aggregate net income of not less than \$5000, and pay an aggregate tax of \$79.98, or $1\frac{9}{10}$ per cent of their income.

The one leading druggist in the town gives no data on income, but according to appearances it cannot be less than \$2500. He is taxed on a stock of \$1000, paying \$28, or $1\frac{1}{2}$ per cent, as a business tax for the protection and privilege of making that net income.

The grocers of the town are paying on stock in trade, counting in rent as a part of operating expenses, taxes running from $1\frac{1}{4}$ per cent to 2 per cent of the net income from the business.

But the general question will be raised as to whether the professional and wage-earning classes pay taxes indirectly as rent. Rents are determined by the supply and demand for houses, not directly by the amount of the taxes. High taxes will act as a deterrent on the building of houses, and so cause a scarcity and a consequent rise in rent. But the appearance of taxes in rent depends upon the action of many other forces.

In a town steadily increasing in population, making a sharp demand for houses, taxes could be thrown upon the tenant. But in many an old New England town with a declining popu-

lation, the supply of houses is more than sufficient, and the landlord must provide for taxes as best he can. The tenant is bound to pay all the rent that supply and demand for houses permit, be the taxes high or low.

As the classes have been examined they pay as follows:

Farmers with poor farms.	8%-10 % of net income
Farmers with good farms.	10%-12 % of net income
Wage-earners, average	1 % of net income
College professors and administrators.	$\frac{1}{10}$ % of net income
Physicians	$1\frac{1}{10}$ % of net income
The druggist (on stock in trade)	$1\frac{1}{2}$ % of net income
Grocers (on stock in trade)	$1\frac{1}{4}$ % of net income

Now if we should eliminate the element of taxes on dwellings in all cases and reduce the conditions to the per cent of taxes which the classes pay for the opportunity and protection in securing their incomes, allowing them to spend it as they desire, the results would be about as follows:

Farmers of poor class	6 %
Farmers of better class	$7\frac{1}{2}$ %
Wage-earners	$\frac{1}{10}$ %
College professors	$\frac{1}{10}$ %
Physicians	$\frac{1}{10}$ %
Druggists	$1\frac{1}{2}$ %
Grocers	$1\frac{1}{4}$ %

This makes the farmer's case still worse as compared with the professional men. They are evidently bearing several times the burden, according to net income, that the other classes carry. In this connection it is interesting to note that between 1890 and 1900, according to the United States Census reports, 330 towns and large plantations in the State suffered a decline of population of from 1 to 30 per cent. Practically all of the rural communities, except Aroostook, declined, while the cities and industrial centers increased in population. In Waldo County, an almost purely agricultural county, 25 out of 26 towns lost in population from 1 per cent to 25 per cent. The one town gained by a temporary industry. In Lincoln

County 16 towns out of a total of 18 lost population, in Knox County 15 towns out of a total of 17 lost, and so the movement went throughout nearly the whole State.

The heaviest burden falls upon the part of the population least able to bear it, and constitutes one of the forces that are driving the men and women off the Maine farms, and causing the depopulation of rural communities.

The movement from the country to the industrial and commercial centers is world wide, and would take place to a large degree without any taxation on Maine farms; but, with this modern strain upon the rural communities in general, it seems all the more unreasonable and unfair to burden the thin and rocky soil of Maine with taxes heavier than those borne by any other plant for economic gain.

Under some conditions taxes on land can be added to prices of products, but this is not generally true in Maine, because this poor soil is obliged to meet the competition of the richer soils of the West. At home and abroad its products are sold in the local markets side by side with those of the Middle West and South. Not infrequently Chicago beef is sold at the gate of the Maine farmer within sight of his own pasture.

But the Ohio physician cannot compete in the Maine medical practitioners' local field, neither can the Maine manufacturer find such water power in Nebraska.

The taxation of real estate mortgages, when enforced, throws upon the farmer another burden which industrial capital does not have to bear. The stock of manufacturing corporations is not subject to taxation, but the mortgage on a farm is supposed to be taxed, thus giving the farm a double taxation to the extent that rates of interest on farm mortgages are higher than they otherwise would be.

In general the property owner pays the tax, while the man who gets his living without holding legal title to property pretty nearly escapes from contributing directly to the support of the government.

This is strikingly true in the case of special assessments for improvements which must be paid for at once.

In the town studied above a new bridge is to be built, costing the town a probable sum of \$25,000, or 2 per cent on the total

valuation of the town. This bridge must be paid for at once, because the town has well-nigh reached the constitutional limit of indebtedness.

Under these conditions Mr. A., who owns a house valued at \$1000, must pay his \$20, Mr. B., who has twice A's net income, but no property, will pay nothing, etc.

The facts that have been exhibited regarding the relations of various classes to the support of the local government could probably be paralleled in some other States as well. I will now turn to two especially pressing problems of taxation in Maine.

TAXATION OF WILD LANDS

In the minds of most of the people, probably, the taxation of wild lands is considered the most important problem of taxation in that State.

The State has 14,261 square miles, or 9,129,119 acres, of wild lands owned by individuals and corporations, lying mostly in the uninhabited and unincorporated townships of the northern half of the State. Besides these there are several hundred thousand acres of public lands devoted to school and other purposes.

Some of this so-called wild land is wild water. Within the State there are 2300 square miles of lake surface, and many townships are partially under water. However, the assessors always take that into account, and no water is supposed to appear in the valuation of the land. Possibly more than half of this water would be found in the wild land region.

The wild lands are taxed under three systems: first, by the State; second, for general county purposes; and third, by special assessments for roads, etc.

The state tax last year was two and one half mills (.0025) on the dollar, the county tax in the seven wild land counties (1905) averaged one mill and fifty-five hundredths (.00155). The two taxes taken together amounted to a little over four mills on the dollar (.00405). Besides this there are the special assessments for improvements in the matter of roads, etc., which are supposed to enhance the value of the property sufficiently to remunerate the owners for the expense.

The wild lands of the State are valued at \$36,423,301, and

the State received (1906) \$91,058.25 from the tax upon them. The aggregate state and county tax amounts to a trifle over a cent and a half per acre. Thus from one half of the State, or from a tract as large as Massachusetts and Connecticut combined, the State government takes not one half as much as it takes from the Maine Central Railroad alone, not one quarter as much as it takes from the savings banks of the State.

The lands were sold by the State to the lumber interests at a very low price, frequently at a few cents per acre, when they should have been held for actual future settlers or leased for lumbering purposes. This would have given the State a source of almost unlimited, perpetual income, and in the future the settlement and development of the northern half of the State would be assured. As it is, great tracts of land are held by corporations and probably will never be opened for settlement.

These wild lands are increasing in value by leaps and bounds, and will continue to do so indefinitely in the future. They are very promising property in view of the predicted lumber famine and coming scientific forestry.

The only hope the government has for redeeming itself from the great mistake of practically giving away one half of the people's domains, is the power of taxation. The assessed valuation of these lands is said to be very low. The state land agent, in his last report, estimated the spruce standing at 21,500,000,000 feet. Spruce stumpage is worth from \$2 to \$7 per thousand, according to the location, and there is a common saying that it averages \$5 at present. This would make the spruce alone worth \$100,550,000. Then there are the pine, hemlock, fir, and all of the hard woods, besides the land itself.

The immediate value of timber lands, as far as internal conditions are concerned, involves several considerations: first, the kind and condition of the timber; second, the proximity to transportation or floating facilities; third, the improvements in the form of roads; fourth, the fire risks; and finally, the amount of lake or river water included.

There is some good timber in Maine that it would not pay to get out at present, because of distance from transportation

facilities. But after all these things are considered, according to the best data on the subject, the Maine wild lands are valued extremely low, and the value placed upon them now will become more unfair every year that it remains at that figure. If the plan of increasing the rate of taxation and not the valuation is suggested, the owner of wild lands replies that the high rates are justified in civilized communities because of the increased opportunities, comforts and protection which a wild region does not afford. But the benefits of civilization appear in increased valuation more than in higher rates of tax.

Why should property in lumber land, productive and promising above the most of property in Maine, be permitted to escape with an aggregate state and county tax of one cent and six mills per acre? Why should non-resident capitalists, living in other and wealthier States, and waxing rich on the increasing values of Maine lumber lands, pay only one fifth of the average rate of tax assessed on other forms of property within the State?

Let us compare the rate paid on the wild lands with the rate paid by the farmer on his wood lot. In the town studied at the beginning of this paper, swamp land and bush land, good for nothing in particular, with no stand of "firewood," is valued at \$1 per acre, and pays a tax of two cents and eight mills. Common woodlands are valued according to the stand of wood, as high as \$10 an acre, and paying twenty-eight cents per acre.

A wood lot valued at \$4 per acre would pay a tax of \$0.112, or seven times the tax on wild land of the same assessed valuation.

The constitutional reason why these conditions do exist is found in Ch. 9, Sec. 40 of the constitution of Maine. "Lands not exempt and not liable to be assessed in any town, may be taxed by the legislature for a just proportion of all state and county taxes as herein provided for, ordering the state and county taxes upon property liable to be assessed in towns."

This passage has recently been interpreted by the Supreme Court to mean that the State can collect only the same rate of taxes from the unincorporated towns that it assesses upon

the property of the incorporated towns. If the State should get all of its income from other sources, it could lay no tax at all on wild lands, and one half of the State would be without taxation, except for the inconsiderable county tax and possible local improvements, which are very rare.

The government of Maine committed one great act of injustice to its people when it permitted this splendid resource of state and national wealth to slip out of its hands. It will commit another error, second only to the first, if it fails to draw, by taxation, from the great domain of timber, an income commensurate with its wealth and productivity.

The rapid increase in population in America and the still more rapid denuding of her forest lands are conspiring to make the timber lands of Maine more valuable than the average citizen has realized.

The Maine people are extremely negligent of their interests if they allow all of this great increase of wealth, brought about by the growth of population, to be appropriated by the few corporations and individuals who have legal control of the lands. Maine has something like a monopoly share of lumber in the Northeastern States, and with careful handling can greatly benefit the commonwealth, and allow individual enrichment at the same time.

Increased taxation is the only means left for the State to secure her share of this enhanced wealth. But what tax should be placed on the wild lands, even if the constitutional restriction were removed or circumvented? I do not know. No one knows, or can know, until some progress is made in the matter. The exact productivity and net income of Maine land, under scientific forestry, has not been determined. The future of the lumber market cannot be fully known.

Very few people would ask that wild land be taxed the same rate borne by property in the incorporated towns, because of the many uncertainties of value, the chances of fires and the possibility of local assessment. But most men will agree that some advance should be made, either in valuation or rate of taxation.

The final settlement will have to depend upon the judgment of scientific foresters and careful experimentation.

TAXATION OF CORPORATIONS

There are at present in round numbers 6700 corporations, not including public service corporations, banks and insurance companies, which take their life from Maine. The aggregate capitalization of these is about \$3,000,000,000, or seven times the total valuation of the State. The government collects a tax of \$144,650 from these, an average rate of $\frac{1}{100}$ of 1 per cent of the capital stock.

The freedom with which Maine creates and authorizes corporations for visionary purposes with invisible capital is too well known to need description. The openly confessed reason is that the State can make a little money by that method. And if the Telegraphone Corporation with a capital stock of \$10,000,000, or the Gulf Coast Company, with a capital of \$18,000,000, or the Phoenix Gold Mining Company with a capital stock of \$25,000,000, should approach you with a proposition to purchase stock, *caveat emptor*, let the purchaser beware, for the State is relieved of all responsibility for creating piratical corporate bodies which go forth to work their schemes on the public. But let it be remembered also that the average Maine citizen does not realize the position which the government has taken in the creation of questionable corporations.

Public service corporations, including banks and building associations, are taxed generally on the basis of gross receipts. But if the State should collect from the other 6700 corporations $\frac{1}{100}$ of 1 per cent on the capital stock, it would have an income from that source alone far in excess of its present total expenditures.

The stock of manufacturing corporations is not taxed, on the principle that the plants are taxed by the municipalities, and the stock only represents the plant.

The taxation of other stock and money at interest in all forms is in a very unsatisfactory condition.

The second largest city in the State reports \$8100 as the total money at interest, but no bonds or stock, except bank stock, which is reported by the banks directly to the assessors by statutory requirement.

Another city reports \$3075 in stocks, but no money at in-

terest. Here and there through the country districts, honest people will report such property; but the present system of declaration puts a premium on lying, and a burden upon honesty.

Two changes are necessary to rectify the great inequalities of the declaration of personal property and the evil of piratical corporations: first, taxation at the source; and second, a sensible tax upon capital stock which will squeeze the water out of some of the corporations, and will cause the disappearance of the most pneumatic bodies.

PROPOSITIONS FOR REFORMS

These propositions can only be mentioned in this space, not discussed. They are made not with the claim that they can all be put into immediate operation, but to point out the directions in which reform needs to move.

STATE FUNCTIONS EXTENDED

Extended functions of the government in the building of highways and bridges and the superintendency and support of schools has become a modern necessity. The old town system for providing roads and bridges never has provided and never can maintain a network of uniform first class highways, wisely and economically administered. Many small towns are burdened beyond endurance by the cost of long, expensive bridges, which should be built and maintained, at least in part, by the State.

The Maine school system should be reorganized and partially maintained by the State. The funds for these extended functions should be raised from wild lands and great natural resources, which are the heritage of the whole State, and from corporations and inheritance taxes.

THE INHERITANCE TAX

The State now has a level tax of 4 per cent on collateral inheritances, yielding \$69,075 (1905). The chief methods of evasion are by transfer of property before death directly to beneficiaries, or by temporary transfer to a direct heir for distribution to collateral heirs after death. The system needs

improvement: first, by extending the tax to direct heirs; and second, by the introduction of the progressive principle.

I believe that no general transfer tax could be devised, for the protection of the inheritance tax, which would meet with popular approval at present.

A PROFESSIONAL TAX

A glance at the figures in the first division of this paper is sufficient to conclude that the professional men are not contributing to the support of the government according to their ability, paying, if taxes on dwellings be considered, one fifth to one twelfth as much as the farmers; and, eliminating the question of dwellings, one fifteenth to one twentieth as much on net income. This applies not only to physicians and college instructors, but to lawyers, dentists, clergymen and scientists.

Carrying out the same principle of justice, we are led to the general income tax for professionals and non-professionals as well. But the general income tax is at present not practicable in Maine, and may never be desirable.

A professional tax would stimulate interest in civic and political affairs among a class of men frequently inclined to neglect public duties and to give little time or thought to their local governments.

THE POLL TAX

The proposition for a professional tax suggests a modification of the poll tax which might accomplish the taxation of professional men, with that of other propertyless persons of large economic ability.

The principle of the poll tax is well established in Maine, and is generally practical. This fact might be made the basis for two important modifications of the present poll tax: first, the exemption of persons paying a fixed minimum tax on property; and second, the introduction of progression, which would apply the tax according to general classes of occupation or profession, and roughly according to income.

THE BUSINESS TAX

I mention the business tax, not because I see any probability of its adoption, but as a suggestion of an ideal which may some time be followed.

The inequalities of the general property tax appear nowhere more striking than in the taxation of business property. A sawmill, with a few thousand dollars' worth of property on hand April first, will have a rapid turnover of raw material and perhaps a large net income. Near it may be a shoe factory, filled with expensive machinery, making no more net returns, but paying several times the tax of the mill.

On one side of the street is a restaurant or shop with a small stock and rapid turnover of capital, but paying a small tax, while across the street is a great store, paying heavy taxes, and often netting no more than the first-mentioned business.

This is a business and commercial age, and if Adam Smith's principle is to be realized, taxation must be placed so as to reach business according to net returns, and not according to stock on hand on a selected day.

THE GENERAL PROPERTY TAX AS A SOURCE OF STATE REVENUE

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I

THE general property tax is to-day the principal source of revenue in the great majority of States and localities in the American Union. It is a survival of the system of taxation universally adopted under more primitive economic conditions, when property was relatively homogeneous, consisting principally of land and agricultural capital, and constituted an approximately fair test of ability to bear the public burden. The conditions which rendered it tolerable have however long since passed away, and in the present stage of industrial development in the United States it has become utterly inadequate to afford a just and reasonable system of taxation. Ignorance, inertia and ultra conservatism in the realm of state finance can alone explain its retention to the present day; and during the past thirty years constantly increasing evidences of dissatisfaction and protest have appeared on every hand. Numerous state tax commissions have reiterated instances of its unfortunate results in practice; students of finance have exposed the unsound theory on which it rests; the Federal Industrial Commission has urged its abandonment as a state tax; and the principal object of the convention in which we are gathered is undoubtedly to impress upon the country at large a sense of the necessity of doing away with it, and substituting some more rational system.

The purpose of this paper is to present a summary of fact and argument against the general property tax, addressed not so much to this body of experts familiar with the subject, as to the interested public who will be reached by the report of the convention.

II

THE GENERAL PROPERTY TAX IN PRACTICE

The first great defect of the general property tax in actual administration is its lack of uniformity, or failure to affect all property equally, owing to differences in the appraisement by assessors of valuation of individuals. While the law requires that all property shall be rated at its true selling value, the actual practice of assessment varies enormously. Individuals are prompted by self-interest to make as low a return of their property as possible, while boards of assessors are influenced by various motives. Sometimes a local system of rating property at a given fraction of its value may be blindly followed. This is often due to a conscious attempt to enable the locality to get off with a smaller share of the state burden, under the conviction that other localities are following the same practice. Again, the assessors are usually local officials, depending upon public favor for reelection, and the fear of giving offence and losing votes influences their action. Often property that changes hands is assessed on the basis of the recent sale, while other property is left on the books at the old figure. In these and similar ways a great lack of uniformity comes about, often resulting in gross injustice. A given tax rate falling upon one place or person may impose ten or fifteen times the burden that it does upon another. The various inequalities that grow out of such differences in the rate of assessment may be summed up as follows:

1. As between different counties, one bears unjustly a larger proportion of the state tax.
2. As between different towns or cities, one has a heavier burden than another.
3. As between town and county, the burden is unequally distributed. In Georgia real estate in the towns is rated by boards of assessors at pretty close to par on the average; while in the counties it is returned by the owner at one fifth or less of the selling value.
4. As between rich and poor in both town and county, a discrimination invariably exists in favor of the wealthier classes.

The second great defect in the general property tax as actually administered is its failure to reach certain important classes of property. It is notorious that personal property largely escapes taxation. In its more intangible forms, such as stocks, bonds, notes, book debts and mortgages, it is beyond the reach of the most inquisitorial assessor; and some of its more tangible forms, such as stock in trade, household goods, jewelry and personal effects, are extremely hard to assess. This is particularly true in the case of the wealthy classes and in the commercial centers, resulting in still further and greater injustice in the distribution of public burdens. Reports of assessors, tax commissions and tax officials from every State in the Union have repeatedly called attention to the fact that personal property was paying a ridiculously small proportion of the whole tax. Such personal property as is reached usually belongs to those who own real estate and whose names are already on the tax books, while whole classes of people whose fortunes are invested exclusively in personalty escape taxation altogether. When it is realized that the wealth of the nation in personalty exceeds that in the form of real estate, the lamentable failure of the general property tax to conform to the principles of universality and justice may be imagined. It has in fact practically become a tax on real estate, including from five to ten per cent of the personalty held by real estate owners.

A third and from the ethical point of view the greatest evil of the general property tax in practice is the constant and almost irresistible temptation to dishonesty which it places before every property owner. A man inclined to be upright is almost forced into dishonesty by the tax. He knows that personalty almost everywhere escapes. He knows that the tax rate has adjusted itself to this condition, and is two or three times what it would be if all personalty were returned. He sees that if he complies with the law he will have to pay twice or thrice his just share of taxes; and he is indeed of sturdy moral fiber if he does not feel that he is justified in doing as his neighbors, — perhaps devising some sophistical argument to reconcile his conscience to the fraud or perjury involved. As the first step in the downward path usually makes a second

easier, who can tell the extent of the demoralization due to the persistent working of this force?

In the keen competition of commercial and industrial life the rigorously honest men may be driven into failure and eliminated by this process.

A concrete illustration is always interesting; two have recently come to my knowledge. In the first, a man of wealth, whose name is a synonym for business integrity and who is widely known for his generous philanthropy, recently established a chemical fertilizer plant in a county where property is returned by the owner on oath. The fumes from the factory proved destructive to vegetation on a small adjoining farm, and to avoid a damage suit the manufacturer agreed to buy the place. The farmer asked \$2500, to which the manufacturer demurred on the ground that the farm was returned for taxes at only \$500. The farmer looked him squarely in the eye and asked him at what his plant, known to have cost over \$150,000, was returned. It proved to have been given in at \$20,000. The farmer's price was paid without a word.

In the other case a farm in an adjoining county was returned by the owner at its actual value. The tax receiver actually protested, and reduced the figure to the basis of the neighboring property.

Professor Seligman in his "Essays in Taxation" quotes a number of state commissions in regard to this aspect of the tax. One calls it a "tax upon ignorance and honesty." Another speaks of "the mischief wrought in its corrupting and demoralizing influence." An Illinois commission calls the system "debauching to the conscience and subversive of the public morals, — a school for perjury promoted by law." A Connecticut commission says its "demoralization of the public conscience is an evil of the greatest magnitude." A New York report asserts that "it puts a premium on perjury and a penalty on integrity." An Ohio commission declares that "it results in debauching the moral sense and is a school of perjury, imposing unjust burdens on the man who is scrupulously honest." A Cleveland commission says: "The existing system is productive of the gravest injustice; under its sanction grievous wrongs are inflicted on those least able to bear

them; these laws are made the cover and excuse for the grossest oppression and injustice; above all and beyond all, they produce in the community a widespread demoralization; they induce perjury; they invite concealment. The present system is a school of evasion and dishonesty. The attempt to enforce these laws is utterly idle." Similar expressions have come from almost every State.

A fourth evil of the general property tax is that in practice it always throws a heavier proportion of the tax upon the smaller properties, and thus discriminates against the poorer classes. This is due in part to unequal assessment, and in part to the escape of intangible property. A house and lot worth \$1000 is inevitably assessed at a figure much nearer its true value than one worth \$20,000 or \$50,000. The simple furniture and personal effects of the former household will be listed nearer their true value, by far, than the luxurious appointments of the house of wealth. Again, the sort of property that notoriously escapes taxation — stocks, bonds, money, notes and mortgages — is in great part the property of the rich, and not of the poor. In this way the general property tax, though nominally proportional in rate, becomes regressive in fact, and imposes the heavier part of the burden of taxation upon those least able to bear it.

A final form of injustice worked by the general property tax is the double taxation that frequently results. Many forms of intangible property — stocks, bonds, notes and mortgages — merely represent the holder's interest in tangible property. To tax both is to tax the same body of wealth twice. This results in practice in confusion, evasion, fraud and oppression. The unfortunate results of the attempt to tax mortgages as well as the full value of the land mortgaged are notorious. The tax is usually shifted to the farmer, in the form of a higher rate of interest. Even where the mortgage escapes the tax assessor, the holder runs the risk of detection, and this is reflected in a higher rate. The widespread depression of farming interests, as contrasted with commercial and industrial prosperity, is largely due to this state of affairs. Several States have attempted to remedy this evil. Maryland exempts mortgages, with good results; and to this extent

has abandoned the general property tax. Massachusetts regards the mortgage as realty, — as an interest in the land, — and allows the mortgagor to deduct the proper proportion of the tax from the interest. The result has been that mortgages in Massachusetts contain a clause by which the landowner is made to agree to pay the whole tax. California has a similar law, and in addition declares such agreements between mortgagor and mortgagee null and void. The only result is that the mortgage rate is 2 per cent higher in California than the general interest rate. Connecticut has exempted such property from taxation on condition that it be registered with the state treasurer, at a fee equal to about one fifth of the ordinary tax rate; but only a small fraction of the owners avail themselves of the privilege. Various forms of debt exemption have been suggested and tried, but have produced intolerable results in practice. The difficulty is inherent in the general property tax. The last report of the Tax Commission of New York, for June 1907, says, "the attempt to apply the general property tax is universally condemned, and it cannot be made fully effective, and therefore cannot be equitable."

III

THE GENERAL PROPERTY TAX IN THEORY

Dr. Richard T. Ely in 1888 published his "Taxation in American States and Cities," fully exposing the inherent defects of the general property tax, and suggesting the lines along which reform must be effected: the separation of state and local taxation; the reservation of realty and certain easily reached forms of personal property for taxation by the local units; the derivation of the state revenue from an income tax supplemented by taxes on corporations, franchises, inheritances and certain minor sources. In 1895 Dr. E. R. A. Seligman issued in form book his scholarly "Essays in Taxation," already known to the academic world through various technical journals, which from the scientific point of view gave the general property tax its *coup de grace*. Both of these books were widely read, and have made the merits of the question familiar to every tyro in taxation. Yet it is an interesting fact that nearly twenty years after Dr. Ely's work, and twelve

after Dr. Seligman's, the system remains practically unchanged in all save two or three of the commonwealths. Why is this the case? Dissatisfaction is on the increase. Numerous tax commissions have been appointed to investigate and suggest relief. But in nearly every instance their recommendations look merely to a more stringent enforcement of the old laws, in the desperate attempt to reach all classes of property by centrally appointed assessors, armed with inquisitorial powers, and backed by the threat of severe penalties for fraud or evasion. And in nearly every case their report perishes stillborn, and the old conditions continue. One reason for this state of affairs may be found in the belief that the imperfect enforcement of the general property tax is the real cause of the trouble, and that if means can only be devised to reach and assess all property, the ends of justice would be attained. Experience has amply demonstrated the virtual impossibility of such an assessment; but we have still to examine the theory and see whether a just distribution of the public burden would be effected if we assume that a complete assessment of all property, real and personal, at its true value, could be obtained.

There is no question that justice in taxation means the levying of the tax in proportion to faculty, to the ability of the citizen to pay. And this faculty or ability is determined by the amount of his net income. Judged by these firmly established principles, the general property tax is unjust in theory, because

(1) Large classes of persons whose incomes are derived from salaries or wages, and who are perfectly able to bear some share of the public burden, are relieved of taxation entirely. A poor man scarcely able to make both ends meet may be heavily taxed on his little home and scanty furniture, while a corporation lawyer making \$25,000 a year, living at his luxurious hotel or club, goes scot free. This is manifestly unjust. Salaried classes should certainly contribute to the support of the State.

(2) Property is a very imperfect test of ability. Some classes of property not only produce no income, but constitute in themselves a drain upon income, such as costly residences and expensive interiors. The only excuse for taxing them is

that they afford indirect evidence of the existence of incomes adequate to their maintenance. But such evidence is only approximate at best, and may be far from correct. It may in many cases be both unjust and bad public policy to discourage by taxation the improvement in the citizens' domestic environment.

Again, of two pieces of lucrative property representing the same investment of capital, one may be far less productive than the other. \$10,000 invested in one way may be producing \$800 a year and in another only \$300. A 2 per cent property tax would require each to pay \$200 — equivalent to an income tax of 25 per cent in the one case and over 66 per cent in the other. I know of the case of a house and lot in Baltimore assessed at about \$6000 which in twenty years has produced a net rental of something less than \$200 a year. The taxes have ranged from \$95 to \$130 a year, a percentage on income of from 50 to 65 — truly unjust and exorbitant. Of two business enterprises of the same capital, one may be barely making expenses, and the other earning handsome dividends, yet each is called upon for the same tax. Again, in a prosperous year a business may make large profits and in hard times may run at an actual loss, and yet by the merciless injustice of the property tax be called upon for the same contribution in the critical time as in the prosperous. In general, unproductive property does not contribute to the owner's ability and should not be taxed, save in exceptional cases like land held for speculative purposes, — exceptions which really prove the rule. But this tax, in theory at any rate, treats all property alike.

The principle of the general property tax further involves, as shown above, double taxation upon certain classes of property owners, which is essentially unjust.

The conclusion is inevitable that the theory of the general property tax is unsound: it assumes that property is a uniform measure of ability, which is untrue; it exempts certain classes from any share of the public burden; and it imposes without reason a double portion upon others. If it were possible to carry it out to the letter in practice, it would still involve flagrant injustice.

IV

THE REMEDY

We have seen that under growing dissatisfaction with the obvious results of the old system tax commissions have been from time to time appointed by the various States to discover a remedy. We have seen, too, that most of these, under the influence of ultra-conservative feeling, have reported plans for the more rigid enforcement of the law. In most cases the legislatures failed to adopt their reports. Where the attempt was made, only greater evil was the result. Perhaps the most strenuous effort to enforce the general property tax is to be found in Ohio, under the well-named "tax inquisitor system," which had the unhappy result of bringing practically no additional revenue into the treasury, exasperating the public, and driving a large amount of property out of the State.

In a few of the commonwealths, however, an effort has been made to modify the general property tax in certain particulars. We have already described the mortgage tax of Massachusetts and California. Missouri enacted a law similar to that of California, but making exceptions in regard to quasi-public corporations, which gave grounds for declaring the law unconstitutional under the Fourteenth Amendment. The Connecticut system of taxing credits has also been spoken of. State boards of equalization to reduce the assessments in the several counties to a uniform basis have been widely tried, but with no very satisfactory results. Another proposal to meet the same end is to assess state taxes on the counties in proportion to the amounts they raise for local purposes. This plan has the endorsement of the New York Chamber of Commerce, the New York State Commerce Convention, the League of American Municipalities, and of a number of labor organizations. It was adopted by Oregon in 1901 to go into effect in 1905. The Oregon plan provides that each county shall pay such proportion of the state taxes as its average expenditure for five years bears to the average total expenditure of all the counties for the same period. This will doubtless work some improvement, but it meets only one of the difficulties of the general property tax. The best proposal, and the one

indorsed by the Federal Industrial Commission, after an exhaustive inquiry into the conditions, is to separate entirely the sources of state and local revenue, and to abandon the general property tax as a state tax. The state revenue could then be derived from taxes on corporations, franchises, inheritances, incomes and other sources, while the local revenues would be supplied either by the general property tax, as the Industrial Commission suggests, or, better still, from a tax on real estate, supplemented by taxes at perhaps varying rates on certain specified classes of personal property, and certain local business or license taxes. In this way the general property tax would be everywhere abandoned, and its place taken by a system more in accordance with modern views of justice and equity in taxation.

THE SEPARATION OF STATE AND LOCAL REVENUES

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I

THE discontent with the conditions of American taxation is growing apace. The reason is not far to seek. On the one hand, the development of industrial democracy is everywhere creating greater demands upon the public purse for a collective action which shall be in the interests of the entire community; on the other hand, the growth of prosperity and the transition from more primitive economic conditions to those of a complex industrial society are rendering more and more inadequate the fiscal basis and the fiscal machinery which have been bequeathed to us by our ancestors. Thus at both ends the pressure is felt. The fiscal needs are multiplied and the fiscal machinery is getting out of gear. Expenditures are growing, and the old forms of revenue are no longer suitable. Hence the pressure of public needs upon public resources. And since these public needs are augmenting most rapidly in the domain of local rather than of national government, it is primarily questions of state and local revenues that are becoming increasingly embarrassing.

It would be a mistake, however, to suppose that the public resources are in themselves inadequate. The fault does not lie with the social income. National prosperity is great and growing, and the increase of wealth and of social income is proceeding unchecked. Were our state and local resources marshaled and organized for fiscal purposes as is done by the national government, the embarrassment would soon vanish. We all know that in normal times there has never been the slightest difficulty in securing a revenue for national purposes which should be, not only abundant, but on the whole satis-

factory to the community. We know equally well, however, that what has been so successfully done by the national government is very imperfectly accomplished by our state and local governments. The wealth is there, the resources are there, but the method of tapping the resources has become unsatisfactory, lopsided and unequal. What is needed is a readjustment of the system to make it fit modern necessities.

In an empire like the United States the problem will naturally assume a somewhat different form in various sections. Finance and politics are but the ultimate expression of economic forces and relations, and the economic conditions vary widely throughout our country. The transition from the frontier life and the activity of a purely agricultural community to the conditions of a highly developed and complex industrial community has made far more progress in some sections than in others, and to the extent that this transition has only begun, the older methods possess a certain measure of validity. What is good for New York is not necessarily good for Mississippi, nor again for Utah. But notwithstanding this diversity of economic conditions, there are certain phenomena which are common to all. The large corporate agencies of transportation are found throughout the country. Some of the great trusts are selling their products in the little hamlets as well as in the important commercial centers. Certain defects in our fiscal system are therefore being recognized as common to the whole country, and with the development of more homogeneous economic conditions this is bound to be increasingly true in the future. We have tax commissions wrestling with very much the same problems, not only in Massachusetts and New York, but in Minnesota and Wisconsin; not only in Louisiana, but on the Pacific slope.

What, then, are the chief difficulties in our tax system which are coming more and more to be recognized everywhere throughout the length and breadth of the land. I should sum them up under eight heads.

First and foremost is the breakdown of the general property tax, which is almost everywhere still the chief reliance of state and local government. The general property tax works well only amid most primitive economic conditions for which alone

it was calculated. Almost everywhere, for reasons which it is unnecessary here to recapitulate, and which it is utterly impossible to prevent, personalty is slipping from under. The administration of the general property tax is everywhere attended with increasing difficulty, and in our large industrial centers it has become, to use the words of a recent tax report, "a howling farce." Everywhere, north and south, east and west, although in varying degree, comes the cry that the attempt to enforce the general property tax, whether by listing bills or tax ferrets, by oaths or by inquisitors, is doing much to force upon the average citizen habits of falsehood and corruption.

Second, a growing lack of equality in tax burdens, not only as between classes in the community, but as between individuals of the same class. Where land, for instance, is assessed at 20 per cent of its value in certain counties, and at 80 per cent or 100 per cent in other counties, it is obvious that the contribution to the state tax is grossly unequal and unfair.

Third, the application to general purposes of what was intended to be only a local revenue. All direct taxation was originally local in character, and the assessment of property for local taxation was at the outset a comparatively simple matter. When the need for state revenues made itself felt, it was obviously expedient to tack on to this local taxation a quota for general purposes. But with the great development of state functions, and with the breakdown of the local barriers of commerce and industry, what was originally equal soon turned into inequality, and the attempt to fetter interlocal or even interstate business conditions by the bonds of purely local assessment has proved to be a fruitful source of difficulty.

Fourth, the failure to make modern corporations bear their fair share of taxation. The corporation is a growth of the last half century. It was unknown when the present framework of our tax system was established. The attempt to force the new wine into the old bottles is not only spoiling the wine, but cracking the bottles.

Fifth, the failure to secure adequate compensation from individuals and corporations alike for the franchises and privileges that are granted by the community. An earnest effort is being made at present throughout the length and breadth of

the land to repair this defect. But with the historic system as it has come down to us in this country of estimating wealth in terms of property rather than, as abroad, in terms of income, we have been plunged into the vortex of the assessment of franchises, and have thus been compelled to attack a problem which does not even exist in other parts of the world.

Sixth, the undue burden cast upon the farmer. Practically, this is the problem of taxation in many of our rural districts and in all agricultural communities where the failure of an adequate revenue system and of the readjustment of social resources makes it impossible to secure good schools or fairly decent roads without overburdening what is, after all, the chief source of American prosperity.

Seventh, the interference with business, due to the partial and spasmodic enforcement of antiquated laws. Witness the attempt in some States suddenly to levy the mortgage tax, as recently in New York, where the entire building industry was thrown into confusion; or the attempt in other States to enforce now this and now that kind of property tax on businesses which led to a change in the location of the business rather than to any increase of revenue. The harassing of the individual business or the fear of harassment is becoming less and less defensible in the delicately adjusted mechanism of modern business society. Over a century ago Alexander Hamilton, in his famous report on manufactures, stated this golden maxim: "All taxes which proceed according to the amount of capital supposed to be employed in a business are inevitably hurtful to industry and are particularly inimical to the success of manufacturing industry and ought carefully to be avoided by a government which desires to promote it. It is in vain that the evil may be endeavored to be mitigated by leaving it, in the first instance, in the option of the party to be taxed to declare the amount of his capital or profits."

Eighth, the failure to make great wealth contribute its due share. In former times, where property was fairly equally distributed and conditions simple, inequalities in tax burdens were slight and unperceived. Before the huge aggregations of modern wealth, the crude tax machinery of earlier days stands impotent. And yet we hug ourselves with the delusion that

all that is necessary is to patch up the old machinery, whereas what is really needed is to throw the old machinery on the scrap heap and to utilize entirely new and modern instruments and processes.

II

We must recognize the fact, however, that revolutions of this kind occur but seldom. The only method of achieving substantial progress in society is, after all, by attempting to go forward step by step. But however slow the change, it is imperative that the goal be kept clearly in mind if there is to be any progress at all. If we move step by step, it is highly important that each step be a forward, and not a retrograde, one. Now the starting point from which progress of all kinds must set out is at the present time in the United States the abandonment of the use of the identical revenue for state and local purposes. Whatever other reforms are needed, and they are many, no lasting progress can be made unless we take this preliminary step. It is for this reason that I have ventured to put in the foreground of discussion the problem of the separation of state and local revenues.

The utilization of the same sources for both purposes is, as we have seen, a natural development, at least in Anglo-Saxon communities where the spirit of self-government has always been strong, and where the local unit has been the cell that has grown through accretion into a mighty nation. Yet the employment of the identical sources of revenue for state and local purposes has not only engendered all the difficulties which have been adverted to above, but has succeeded in confusing the issue, and in rendering almost impossible a satisfactory solution of the problem. Where each local community finds that its interests are in some unaccountable way bound up with those of other communities, the tendency is to induce an unwillingness to experiment with any changes, no matter how necessary, which through the influence of these common interests may perhaps react disadvantageously upon the interests of the particular community. The result is the breeding of mutual suspicion and, what is still worse, of lethargy. Just as no single individual can be expected to submit an accurate

list of his taxable property when he is absolutely sure that his neighbors are all successfully withholding their own, so no community will be willing to make any change in methods, the result of which would, in all probability, only be to increase its common burdens. The separation of state and local revenues is therefore a matter of vital importance in the American commonwealths of to-day, not so much because it forms in itself any solution of the problem, but because it is the indispensable initial step to any substantial progress. The separation of state and local revenues is not a cure, but it alone will make a cure possible. It is from this point of view that we must address ourselves to the problem.

There are four aspects of the subject: First, what is meant by separation of state and local revenues? Second, what are its disadvantages? Third, what are its history and development? And fourth, what are the dangers of the system?

I. In the first place, separation denotes, as the word implies, some distinction between the classes of revenue. Almost everywhere in the United States the general property of individuals is assessed for local purposes, and as corporations developed, their property was also assessed in the same way by local assessors. County expenses are usually defrayed by apportioning the necessary amount to the localities according to the assessed valuation of property and thus adding a county rate to the local rate. Finally, the state expenditures are defrayed in precisely the same way by dividing up among the separate counties a sum proportioned to the assessed valuation in the counties. Thus the final tax rate upon property is made up of the addition of these various rates. But the assessment and the collection are for the most part in the hands of local authorities.

What will be gained by the separation of state and local revenues is that the state revenues will no longer be collected from the same source and in the same manner as the local revenues. It means practically that there should be no state tax rate on general property added to the local tax rate through the process of apportioning state expenditures among the localities according to the assessed valuation. And it implies as a corollary that some other method of securing the state revenues be

devised. The demand for separation is primarily a negative rather than a positive one; it is destructive rather than constructive. It claims that the root of the present evil must at all costs be pulled out. It leaves open for debate what particular alternative methods should be substituted. It proclaims in no uncertain tones, "Leave to the locality what properly belongs to the locality; allot to the State what properly belongs to the State."

II. The second aspect of the problem is a discussion of the advantages that would ensue from separation. These may be summed up under the following heads: *A.* Conformity with the natural division of government functions and activities. *B.* Greater equality in assessments. *C.* Lowering of the tax rates. *D.* Removal of conflicts between city and county. *E.* Greater flexibility and adaptation of means to end.

A. The first advantage is the conformity with the natural division of government functions and activities. The relation of government to business life necessarily changes with the conditions of business activity. When business was purely local in character, as was true in former times, the local authorities were competent to deal with them. To-day yet, activities connected with real estate are still largely of this character. The real estate cannot be removed from the locality, and the benefits and burdens attaching to real estate are still to a very large extent bound up with the people who live in the immediate neighborhood. What is true of real estate was originally true of almost all economic phenomena. But it is no longer true. The scope of the great industries connected with the transportation of wealth and the transmission of power or intelligence is obviously no longer local in character, and many of the ordinary corporations and businesses are stretching out with an activity that transcends all local bounds. While the central office must indeed be in some one locality, the scope and content of the activities are no longer local, and in the great majority of cases any attempt to estimate the economic capacity of the business or corporation to bear the tax burdens by the property existing in that locality would be woefully inaccurate. Not only would the local property often be in no proportion at all to the local sales, but even the local sales would

not be any index of the relative profits or tax-paying ability. The insurance company (although situated with its head office in some one town) does business throughout the entire State; the railroad may have four tracks in a little country village which contributes practically nothing to the traffic; a bank may derive its profits in large measure from out-of-town business. Where the activity is primarily interlocal or state, the burden should be interlocal or state.

Not only, however, is there this natural division between state and local functions, but even where the phenomenon itself is purely local, experience has disclosed in some cases the great advantage of assessment by state rather than by local officials. Real estate, for instance, can far better be valued by officials of the neighborhood who are cognizant of the local conditions. But the administration of a liquor license law is apt to be far more effective if divorced from local influences. It is for such a reason, for instance, that the liquor-license tax is now levied in New York by state officials with a far greater degree of efficiency and therefore with a far greater resultant revenue than was formerly the case. So also certain taxes are more effective when resting on a broad than on a narrow basis of assessment. The inheritance tax, for example, is obviously unfit for a source of local revenue because the number of wealthy individuals who die in any one year in a single town or city is so unpredictable and oscillating that the revenue would be entirely too spasmodic. Broaden the base by taking in the whole State, and the amount of property passing by death from year to year will be found to fluctuate very little.

Thus, from the double point of view of historic changes in the scope of government functions and in the effectiveness of administration, a clear line can often be drawn between what is properly a state and what is properly a local source of revenue.

This consideration really carries one step farther a distinction which is found almost from the beginning of our national existence. At first, there was no line drawn between national and state sources of revenue, and in the critical years succeeding the Revolution the Union had to depend upon requisitions addressed to the separate States to be raised by them in the

same way as their own local revenues. With the collapse of this system was settled once and for all the principle of a separate and independent national revenue from sources, in part at least, distinct from those of state revenue. The whole domain of foreign commerce, which up to that time had been within the purview of the separate States, was now transferred to the Union, and the force of historical necessity has since then converted certain forms of internal taxation, which were still for a long time administered by the separate States, to the practically exclusive possession of the Union. The process is not indeed entirely complete, and we are even now debating whether certain forms of state taxation should not hereafter be relegated to the general government. The point which it is desired here to emphasize, however, is that the principle has been settled. It is the same principle which is now applicable to the separation of revenues within the State. It was the financial collapse of the Confederacy which brought about the separation of national and state revenues. It is the practical collapse of our antiquated fiscal system within the States which is just beginning to bring about the separation of state and local revenues. The change in the economic conditions at the end of the eighteenth century was responsible for the one; the change in the economic conditions at the beginning of the twentieth century will be responsible for the other. Thus, the first advantages of the separation of state and local revenues is the fact that it is in harmony with an underlying principle of historical growth.

B. The second advantage is the securing of greater equality in assessments. The differences in assessed valuations in various sections of our States have everywhere become so glaring that the last few decades have seen in almost every case the creation of boards of equalization designed to remedy the acknowledged evil. It is equally notorious, however, that the remedy has been entirely inadequate and that the boards of equalization have been unable to accomplish what was expected of them. The inequalities go on almost unchecked, very largely for the reason that the members of the state boards have too imperfect a knowledge of the local conditions to admit of any successful revision of property valuations.

The relegation of the general property tax to the localities will at once render unnecessary any equalization, for if the state revenues are secured in other ways, and if the general property of individuals, whether real estate or personalty, is not directly liable for state purposes, there will of course be no inducement for the local authorities to seek to lower the local valuations of property. For purely local purposes it makes no difference whether there is a low valuation with a high tax rate or a high valuation with a low tax rate; the result is precisely the same. With the separation of state and local revenues the individual landowner in one part of the State will no longer be casting envious glances at the landowners in other parts of the State, and this mad scramble for reduction of assessments will be checked. It will depend entirely upon the people in the community itself, and not upon those in other communities, whether the individual tax rate shall be high or low.

C. This brings us to the third advantage, the political aspect of which is not slight. Where, as at present in some cases, the state taxes form no inconsiderable part of the whole, the tax rate upon the individual property owner is naturally augmented to this extent. Under a system of separation of state and local revenues, with a relegation of the property tax to the localities, the rate of the tax will naturally be lowered by the entire amount of the state revenue previously derived from this source. In the development of the system in New York, for instance, this argument had great weight with the legislators and was largely responsible for achieving the final result. The separation of state and local revenue means a reduction of direct taxation of property.

D. The fourth advantage is the removal of conflicts between city and county. The present situation in many of our States is really an outgrowth of point *B* mentioned above; namely, the inequality in the assessments of property. Many of the rural counties claim that since there is a far larger proportion of tangible and visible property within their borders than is the case in the larger cities, the property actually assessed in their case greatly transcends in its relative proportions the property assessed in the cities. There is, therefore, a frequent

pressure upon boards of equalization to raise the total valuations in the cities and to compensate for this by reducing the valuations of the rural districts. In a State like New York, for instance, there was an almost annual contest marked by bitterness and asperity, leading in some cases to the threat on the part of the city of New York that an attempt would be made to create a separate State. The separation of state and local revenues puts with one blow an end to all these sources of difficulty and friction. The large city as well as the small town, each is allowed to go its way in peace.

E. The final advantage is virtually a corollary of the one just discussed; namely, a greater flexibility and adaptation of means to end. If each locality is now, through the separation of state and local revenues, divorced from the others and is left to work out its fiscal salvation, to a certain extent at least, independently, it is obvious that each locality will be better able to adjust its fiscal system to its own particular fiscal needs. The conditions of a commercial metropolis are very different from those of a country hamlet, and what may be entirely appropriate in the second case may be found to be completely unworkable in the first. The slow steed and the fleet pacer work very ill together in harness: set each of them free to do what he can and the total result will be far more satisfactory for all concerned. Uniformity of fiscal methods is desirable only where there is a uniformity of economic conditions. If we allow the different localities to experiment, within certain broad lines, as to the fiscal methods best suited to their own prosperity, the result is ultimately bound to be an adaptation of fiscal practice to economic fact.

Thus from each of these five points of view the benefits which would accrue from a separation of state and local revenues are clear and undeniable. But so strong is the force of custom and prejudice, and so inadequate is the ordinary analysis made of the situation, that the movement has really only just begun in the United States.

III. We come then, in the third place, to a word as to the history of the separation of state and local revenues.

The separation of state and local revenues in the sense of abandonment of the general property tax for state purposes

has been achieved in only one important commonwealth, New York. In several States, indeed, a beginning has been made by securing for state purposes a supplementary revenue over and above that from the general property tax. But this partial achievement virtually secures none of the advantages of a complete separation except possibly that of a moderate reduction in the tax rate. It is valuable only as affording a basis on which to erect the complete structure of an independent state revenue. Again, in a few of the smaller Eastern States, like New Jersey, Connecticut and Delaware, where the state expenses are relatively slight, it has been found practicable to defray the state expenses primarily from taxes on corporations. But even here the separation of state from local revenue is ostensible rather than real because as in New Jersey the school taxes, which do not figure in the state budget, are divided by the State in proportion to local valuations on property, thus virtually continuing all the disadvantages of a state assessment or a state equalization. Pennsylvania has almost reached the goal by discontinuing any state taxation of real property, but Pennsylvania still enforces the state tax upon personalty, even though this be done in a somewhat peculiar way. New York is the real example of separation of state and local revenues, although from the local point of view the separation is not complete because corporations are still nominally subject to the general property tax for local purposes. So far, however, as the chief point is concerned, namely, the abandonment of the general property tax for state purposes, New York has in practice reached the separation of state and local revenues.

This has been accomplished only within a year or two. The creation of an additional and supplementary source of state revenue over and above that from the general property tax began almost a quarter of a century ago, but it was not until about a decade later that the author of this paper was fortunate enough in impressing upon the authorities the importance of a system of complete separation. Ever since that time the process has gone slowly forward, until in 1906 the last step was taken and provision was made for securing the entire state revenue — between thirty and forty millions of dollars — from

other sources than the general property tax. The separation, however, is not yet enforced by any specific law; it is simply the result of annual legislative decision. In New York, therefore, we stand on the threshold of a far more important movement. We have cleared the way and are ready to begin our onward march. What has been accomplished in New York is certainly not impossible of accomplishment elsewhere.

IV. It may be inquired, however, in the last place, are there no objections to the system of separation or are there no dangers connected with it? A candid consideration would compel an answer in the affirmative, but a closer scrutiny will result, I think, in the conclusion that the objections are largely specious, and that the dangers are at least remediable.

What are its objections and dangers? They may be summed up under three heads: a lack of suitable state revenues; a lack of elasticity; a lack of suitable local revenues. Let us consider these in turn.

It might be claimed by some States that if the general property tax is abandoned as a source of state revenue, there is nothing to put in its place. The experience of the more advanced States, however, shows the fallacy of this contention. Even where the ordinary business corporations have not assumed vast proportions, we find in all the States the existence of the great public service corporations. Under a proper system of assessment, the tax on corporations of this kind, if reserved primarily for the State, would go far toward defraying all legitimate state expenses. The difficulty now is that in many of our States the greater part of the taxes on corporations go to the localities, where, as we shall see in a moment, they are not needed, and only a small part, if any, is assigned to the State. If we render to Cæsar what belongs to Cæsar, the tax on corporations will go primarily to the States. Another source of state revenue which is now spreading in this country, but which has by no means received the development of which it is susceptible, is the inheritance tax. In New York over one sixth of the entire state revenue is secured from this source, and the same is true in many foreign countries. Owing to defects in the principle as well as in the administration of the law, the inheritance tax in many other

States is very ineffective. But New York again has shown the way. Where corporations and inheritance taxes do not suffice, other sources of revenue stand ready at hand. There is no reason, as we have seen above, why the license taxes should be reserved exclusively for local purposes. In the Southern States the license or occupation taxes have for a long time gone, in part at least, to the State, although the whole Southern system is capable of much improvement in this and other respects. Here, again, in New York, it has been shown what can be done, and about one third of the entire state revenue comes from the liquor license tax alone. In short, without going more in detail into this question, which is susceptible of a far larger treatment, it may be said that there is scarcely a State in this Union where, under proper methods, adequate sources of state revenues could not be discovered and effectively employed. But even if this were not the case, and if it turned out to be difficult to secure additional sources of state revenue, there is still left a simple and efficacious means of accomplishing all the advantages that can be derived from separation, without incurring the hazard of not finding sufficient state revenues. This method may be called the apportionment-by-expenditure method.

The apportionment-by-expenditure method may be described as follows: At present the state general property tax is distributed among the counties by apportioning the quota of each according to the assessed valuation of property. The apportionment-by-expenditure method as opposed to the apportionment-by-valuation method would distribute the amount to be raised for state purposes to each county on the basis of the total expenditure or, what is the same thing, on the basis of the total revenues collected to defray this expenditure within each county and all the taxing districts contained in the county. The advantages of this scheme are obvious.

First and foremost, it would permit each locality to raise its revenues as it chose within certain broad lines, as laid down by the general law. The apportionment being no longer according to the valuation of property in general, but according to expenditures or revenues, it would be immaterial to any section in the State how the local revenues of any other sec-

tion were raised. The important point would be the extent of the revenue and not the manner of raising it.

It was mainly to secure at once local option in the selection of the subjects of taxation that the apportionment-by-expenditure method was urged by Mr. Lawson Purdy, who first suggested this scheme several years ago.¹ This designation of local option is perhaps not entirely happy in that it does not adequately describe the powers to be conferred upon local communities. Moreover, the term "local option" has become so intimately associated with the liquor problem that its utilization for taxation is apt to become confusing.

Secondly, even if the general property tax were retained for the basis of assessment by the localities, the apportionment-by-expenditure method would result in a more equitable distribution of the burden than is the case at present. For, as has been explained, it is notorious that assessments of personal property in the rural counties are almost inevitably higher when compared to actual values than is the case in the cities. On the other hand, expenditures or revenues correspond much more nearly to the actual taxable abilities of the communities. Hence, apportionment by expenditure would bring about a more equitable distribution of burdens than is the case at present. A careful computation that was made several years ago in New York when the board of equalization still apportioned the state tax shows that under this new system the counties which would pay more are either the rich counties which contain the most valuable land in the State, or the counties which received too high a percentage rating from the board of equalization.²

Thirdly, the apportionment-by-expenditure method would tend to economy in both state and local government. Local extravagance would, to a slight degree at least, increase the proportion of the state burden, and state extravagance would be directly reflected in a higher charge on the localities.

¹ "Local Option in Taxation," a paper read at the Buffalo National Tax Conference, May 23-25, 1901; also separately published by the New York Tax Reform Association. In this paper, however, Mr. Purdy is perhaps unduly critical of the other method of securing separation of state and local revenue.

² The figures are given in an appendix.

The fourth benefit is that the present state boards of equalization would be rendered entirely unnecessary, for the whole matter would be settled by a mere arithmetical computation which would leave no room either for favoritism or for unintentional injustice.

Finally, fifthly, since it would be necessary to have full figures of statistics and revenues of all counties and local divisions, we should secure at once a system of comparative local statistics which have hitherto been almost entirely wanting in most of the States, and the lack of which is a serious obstacle to fiscal form.

The chief objection to this scheme of apportionment by expenditure is that it might tend unduly to prevent desirable expenditures in the more progressive communities. The force of this objection is, however, not so great as it seems. For, in the first place, if the community is ready to subject itself to the burdens of a larger expenditure for desirable aims, it will scarcely be checked by the very slight additional burden which would result from the increase of the state tax. For the local burden is always very much greater than the state burden. Secondly, even if this were not true, the force of the objection could be very largely attenuated by combining the apportionment-by-expenditure method with the system above described of an independent state revenue from other sources than property. If this were done, that is, if the greater part of state revenues were derived from independent taxes, and if only the necessary residuum were raised by the apportionment-by-expenditure method, the proportion falling to each locality would be so exceedingly slight as virtually to rob the objection of whatever strength it might be supposed to possess.

It is interesting to observe that the apportionment-by-expenditure method has been introduced into one State, namely, Oregon. The Oregon law of 1901 adopted the scheme, however, only in part, in that it apportioned the state property tax to the counties for the first few years according to a table of fixed percentages based on valuations. According to the new law of 1907, the system of apportioning taxes according to expenditures is to go into effect in 1912. In Oregon, however,

there are two points in which we find a departure from the principles of the system. The first is that the apportionment is not to be made according to all expenditures, but only according to some expenditures, — expenditures for roads, for interest on the debt, for courthouses and for fighting pestilence being deducted in each case. More important than this, however, is the adoption of the rule that the apportionment itself is to be made according to county expenses instead of according to the total expenses of all the localities within the county as well as of the county itself. While something perhaps may be said for the first derogation from the principle, it is difficult to see the justification for the second. For in this way the apportionment-by-expenditure method is robbed of many of its advantages. Even this partial adoption, however, of the system secures for Oregon the great object which was to be attained; namely, the separation of state and local revenues. It must also be remembered that Oregon joins to the apportionment-by-expenditure method that of independent state revenues by special taxes.

Thus we see that the contention that separation of state and local revenues is impossible in some States, because of a lack of adequate state revenues, is weakened, if not entirely overcome, by the adoption, in part at least, of the alternative method to be employed in one of the least developed of our commonwealths. It must, however, not be supposed that the principle of separation of state and local revenue is conditioned by the acceptance of the apportionment-by-expenditure method. If this method should on the whole prove to be unwise or inexpedient, the separation of state and local revenue would not be affected thereby. The separation of state and local revenue does not necessarily imply either complete local option or any specific method of apportionment. These do not stand or fall together.

The second possible objection to the scheme of separation is the lack of elasticity in state revenues. Whatever are the drawbacks of the general property tax for state purposes, it is undeniable that the system is a highly elastic one. When the State needs more revenue, it simply increases the tax rate; when it needs less revenue, it diminishes the tax rate. By

abandoning the general property tax for state purposes, we therefore lose this necessary element in the system.

There are, however, three ways of reintroducing the elasticity which will be lost. The one obvious and simple method is to utilize as the elastic feature the apportionment-by-expenditure method just described. If any more money is needed in any one year, so much more can be apportioned to the counties. Secondly, in default of the adoption of this method, the elasticity lost by the abandonment of the general property tax for state purposes might be regained by introducing a varying rate in one of the other taxes. There is no necessary reason why the tax rate should always be the same from year to year. In the case of taxes on business or on corporations, indeed, it would be highly inadvisable to alter the rates from year to year as tending to unsettle business. But to other forms of taxation this objection would not apply. England secures elasticity by varying the rate of the income tax from year to year. There is no reason why in the American States the rate on the inheritance tax should not be modified from time to time so as to secure a slightly greater or slightly smaller revenue. The change in the tax rate on inheritances cannot very well bring about a change in the death rate of the people whose property is inherited. And thirdly, even if neither of the above schemes approves itself to the community, we might adopt the suggestion which has been made in the recent report of the New York State Tax Commission; namely, that the State should accumulate a small surplus which it would hold to meet any possible deficit, and that when the surplus exceeded a certain figure, it should be automatically returned to the localities for the relief of local taxation.

In any one of these three ways elasticity could surely be secured.

The third and final objection to the separation of state and local revenues is that the localities cannot afford to relinquish to the State any sources of revenue which they now possess. It is claimed, for instance, that many of the rural counties which now secure a large revenue from the property tax on the property of the transportation companies which happen to traverse them cannot afford to lose this revenue.

We here come to a point which has been much neglected in the discussion of the subject; namely, an insufficient analysis of what is really implied in the separation of state and local revenues.

As I conceive it, there are two kinds of separation which might be termed respectively the segregation of source and the division of yield. The segregation of source means that an entirely different source of revenue should be utilized for state purposes from that which is used for local purposes. It is this which is meant when we say that the State should no longer derive its revenue from the source of the general property tax. But there is an entirely different method of attaining the same result; namely, by the exclusive state assessment of certain sources of revenue coupled, however, with an apportionment of a part of the proceeds to the localities. For instance, the inheritance tax ought to be levied by the State and not by the locality; therefore there would be here a segregation of source in the assessment. There is, however, no reason why, after the tax has been collected, a part of the proceeds should not be apportioned to the localities. The corporation tax ought indeed to be levied independently by the State, and here again there is no reason why a portion of the proceeds should not be distributed to the localities. The excise tax in New York is admirably administered by the state officials, yet one half of the proceeds is returned to the localities. The division of yield of a tax is perfectly compatible with a segregation of the source of a tax. The trouble with our present system is that we attempt to make a local assessment of all property and then add something for the State, thus producing all the evils of the actual situation. What should be done, and what is beginning to be done in some places, is to leave the property tax on individuals entirely to the local divisions and to develop a system of taxation assessed in first instance by the State, but with an apportionment among the localities of so much of the proceeds as may be necessary. We must not confuse segregation of source with division of yield. If we establish a separate system of state taxes, that is, a tax levied and assessed in first instance by the State, and if we then find, as can easily be accomplished, that the revenue is more

than adequate for state purposes, it is an exceedingly simple matter to arrange for a distribution of the overplus among the localities.

As stated earlier in this paper, the difficulty is not with the social income as a whole. There is in the community an abundance of wealth which has never been tapped. The difficulty lies in the present method of apportioning the burden. By raising local revenues primarily from those sources which exist in abundance in the localities, and which are by nature local in character, and by retaining for state assessment those taxes which have a wider economic basis, we can be just to all demands of both State and locality without imperiling the fiscal situation in either, and at the same time securing a freedom from all the difficulties that beset us at present. The separation of state and local revenues includes two distinct phases, the segregation of the source of revenue and the division of yield of the tax. The real principle is to reserve a direct taxation of property for the localities and to hand over to the State all the important sources of revenue, dividing a part of the proceeds among the localities and possibly making up any part of the deficiency for the State through the system of apportionment by expenditure. In this way we may secure all the advantages of separation of state and local revenue, and yet avoid the dangers and pitfalls.

It will be seen from the above presentation that separation of state and local revenue is by no means identical with what is sometimes called local option in taxation — a term in itself unfortunate for reasons that have been mentioned above. Separation does, indeed, involve some measure of choice by the localities, and that is, in fact, one of its great advantages; but local option may obviously be carried to an extreme. The liberty of taxation on the part of separate local communities must not be permitted to disrupt the general scheme of taxation, or to imperil business activities through a rivalry in the application of the taxing power. What has been so laboriously gained in state taxation through the intervention of the national authority, which prohibits the state taxation of interstate commerce, must not be lost in local taxation through the absence of state control. What the separation of state and local revenue

seeks to accomplish is, as we shall see below, to make it possible for localities ultimately to exempt personal property from taxation. So far as a flexibility of local revenue may render this possible, it is desirable to grant to the locality, at least to this extent, a latitude of exemption. But this is far from being synonymous with a general demand for complete local option. That is a proposition which deserves discussion on its own merits, and to which valid arguments may undoubtedly be opposed. Let us not endanger the attainment of the principle of separation by confounding it with a far more radical system of complete local option.

III

There remains a word to be said about the ultimate outcome of the process of which the separation of state and local revenue is only the first step. To discuss this as it deserves to be discussed would need a separate paper. All that I shall here attempt is to give a faint indication of the probable development.

In a primitive democratic community, the simplest way to reach the taxable ability of the individual is through his property. The general property tax is a satisfactory index of relative taxable faculty because the property is homogeneous. To tax the individual and to tax the property of the individual is virtually the same thing. But in modern times property is no longer homogeneous. With the development of commerce and industry on a vast scale, property splits up into all sorts of forms and the old homogeneity disappears. It becomes practically impossible to reach all forms of property equally. But as soon as it becomes in practice, as it does everywhere, an uneven tax, the social consequences of taxation make themselves felt. The taxation of certain kinds of property is no longer the taxation of the individual who owns the property. He may pay the tax, but he no longer bears the tax. The vast economic forces which affect the property relations of class to class make themselves felt. Some taxes are shifted onward to other classes, and are, perhaps, ultimately diffused throughout the community. Some taxes are shifted backward to the original owner and through the process of capitalization

are discounted by the new purchaser of the property. Thus, while some taxes remain on the owner, others finally disappear entirely as a burden through a process of diffusion or absorption. A tax on mortgages, as is now well understood, does not remain on the lender of the money, but is shifted to the borrower, and where the borrower is a building operator, it affects the dwellings and ultimately the rentals with various incidental consequences all the way along. A tax on city lands is not borne by the man who has purchased the land after the tax is imposed, because he makes allowance for the tax in the purchase price of the land. The same is true of the purchaser of corporate or government bonds. A tax on the stock-in-trade of a merchant or factory-owner, if predictable and applied to all the members of a class, results in an increased price of that commodity to the consumer. No constitutional provision can be of avail against the overpowering force of economic pressure. We may, like Cnut, order the waves to recede, but they will not recede. The constitutional provision in most of our States, that all property should be taxed alike, has outlived its usefulness. You cannot tax all property alike, because it is humanly impossible under modern conditions to reach all property alike; and if you do reach all property alike, the modern social effects of taxation are such that you would not be putting an equal burden upon the property owners because you would then be hitting the wrong man. Until we recognize the fact that under modern conditions to tax the property is not, in many cases, to reach the owner of the property, no solution of the problem can be attained.

The separation of state and local revenue is, therefore, of such fundamental importance because it will allow every community to approach the problem in an unbiased way, and will enable them to select those classes of property which could profitably be relinquished. It means practically that those communities which choose to abandon the personal methods of taxation and to substitute an impersonal taxation may be permitted to do so.

The two questions that will naturally present themselves here, however, are: first, how will great wealth be made to bear its share, and second, how is the burden on the farmer to be

lightened. As to the first point, it may perhaps be queried whether a better way of reaching great wealth is not by curtailing the special privileges which so often make great wealth possible. Without, however, developing this point here, it may be affirmed that if we desire to reach the results rather than the sources of great wealth, a method stands ready at hand. By developing the inheritance tax we shall accomplish all the advantages of a personal taxation without any of its drawbacks. A state income tax would, under our actual American conditions, not work a whit better than the discredited personal property tax, and the only possible resort to it would be under the ægis of the national government. With the corporation tax and the inheritance tax we shall go far toward reaching the main elements of modern fortunes. The difficulties here, indeed, arising from the conflicts of state jurisdiction are great, but not insuperable. They will be overcome either by the development of a system of interstate comity, or perhaps by a further development of the principle of division of yield, whereby the taxes will be assessed in first instance on a uniform basis by the federal government and then apportioned according to constitutional methods among the States.

The second problem is that of the farmer. If the local tax is primarily on real estate, and if, as frequently happens, the conditions of production are such that the farmer is unable to shift the burden of the tax to the consumer, what can be done? Here a double avenue of escape is open. In the first place, many of the expenditures of local communities ought to be defrayed by the state government. Even now, in several of our commonwealths, state roads are being constructed throughout the local divisions because transportation is being recognized as affecting the interests of the whole State. But if certain roads ought to be state roads, and constructed at state expense, why should not certain schools be state schools and conducted at state expense? Education, like transportation, is more than a merely local matter.

In the second place, while the expenditure side may be cut down in this way, the revenue side may be augmented by an application of the principle of the division of yield whereby the overplus of certain state taxes like the excise tax or the

corporation tax or the inheritance tax is distributed among the localities. Thus the burden on the local real estate will be decreased rather than augmented. Under the present system the farmer pays not only his own taxes, but in large part the taxes of the rich men of the rest of the State. Under the new system of separation of state and local revenue, carried to its logical conclusion, the farmer will pay less and get more; and what is true of the farmer is true of other classes. The tax burden will be shifted from the individual to the economic phenomena themselves.

The problems of taxation in the United States are becoming every year more complex. In order to solve them we must keep in mind the ultimate goal, and be prepared to take the first step. The ultimate goal is the accommodation of fiscal methods to our changed economic conditions. The first step is the separation of state and local revenues.

APPENDIX ¹

Apportionment of state taxes in the State of New York on the basis of local expenditure or revenue, compared with apportionment on the basis of the equalized assessment of real and personal property.

Accompanying this memorandum there are two tables, one of which shows the percentage of state taxes charged to each county of the State of New York in 1902, based on the equalized assessment of real estate and the assessment of personal property. The table also shows the percentage of state tax which each county would have been required to pay if the state tax had been apportioned on the basis of the local revenue in 1902, reported by the State Board of Tax Commissioners in their report for 1903. This report is incomplete in that highway taxes are omitted from the reports of towns. This affects the revenue of counties containing no cities more than the revenue of counties which contain cities, as the tax for streets is contained in the total revenue of cities. In the strictly rural counties the highway tax amounts to from 7 per cent to 12 per cent of the total revenue. The percentage of state tax paid by rural counties is so small that the omission of highway taxes affects the percentage very little.

Comparison of the percentage columns shows that the counties containing large and progressive cities, in fact the three richest counties outside the city of New York (Erie, Monroe, and Westchester), and the city of New York itself, would pay a larger share of the state tax if this share were determined by an apportionment on local revenue.

All the other counties which suffer an increase are described in the second table, with the exception of Oneida, Rockland and Saratoga; for Oneida and Saratoga the increase is very slight. Oneida contains prosperous cities, and Saratoga is a great summer watering place; both are prosperous counties. Rock-

¹ Prepared by the New York Tax Reform Association, of which Mr. Lawson Purdy was at the time secretary.

land is a suburban county which to some extent reflects the prosperity of New York.

In the second table a comparison is made between counties whose proportion is decreased and counties which suffer an increase, and so far as possible counties of similar character and nearly equal population are grouped together. For the purpose of comparing the wealth of the counties, the table shows the area in acres, the population in 1900, the "special franchise" assessment, the real estate assessment, and the percentage of full value with which the assessment of the county is credited by the State Board of Equalization.

The special franchise assessment is made by the State Board of Tax Commissioners. It is the assessed value of the property of public service corporations in streets and public places together with the value of the right, privilege or franchise to maintain and operate it there. The value of special franchises is an indication of the density of population and reflects the value of land bordering the public streets. Where the value of land is low, a franchise is not valuable; where franchises are very valuable, the land bordering the highways is valuable.

In the first group it will be noticed that the proportion to be paid by Chautauqua County is increased, and that it is credited with a very high percentage of assessed value. Tried by every test, this percentage seems considerably too high. The value of real estate in Chautauqua is evidently much more than in Jefferson County, and much more than the assessment indicates. Ulster County has land of high value because within it is situated some of the most beautiful scenery of the Catskill Mountains, and it is visited in the summer by many thousands of wealthy people.

In the next group Clinton County is a remarkable example of underassessment, and the percentage rating of 50 per cent is readily seen to be too high when Clinton is compared with Chenango, Greene, and Livingston or with any other county of similar character. Essex and Franklin both have many acres of timber land, especially Essex, which is obviously under-assessed.

Hamilton County stands by itself as a peculiar county. It is narrow and very long, most of it in the Adirondacks.

In Hamilton County there are the summer homes of many wealthy men who own large tracts of forest land. The assessment is low.

In the next group, Schoharie is one of the poorest counties of the State in proportion to its population, yet its assessment is high as compared with many others in the table. Sullivan County is obviously given too high a rating. It has more than double the population of Putnam County, almost three times its franchise value and the assessment is about two thirds. Putnam is a farming county just as Sullivan is.

In the next group, Madison and Washington are farming counties, while Herkimer and Schenectady have considerable manufacturing cities.

In the last group, Dutchess and Orange are farming counties, and Suffolk is unique. It comprises the easterly two thirds of Long Island. It is very poor for ordinary farming purposes, but the north and south shores are becoming valuable for summer homes.

Niagara County has the power of Niagara Falls, is developing great manufacturing establishments, and there is no doubt that the power privileges are greatly underassessed and that the assessment as a rule is not high enough to justify the rating of the State Board of Equalization.

These comparisons show that the counties which would pay more if the state tax were apportioned on local revenue are either rich counties which contain the most valuable land in the State, or are counties which receive too high a percentage rating from the Board of Equalization. The counties which would pay less are poor counties with land of low value, or counties which do not receive the percentage rating to which they are entitled.

STATE OF NEW YORK

Comparisons between some counties, showing in the first column the percentage of state tax paid in 1902, and in the second column the percentage which would have been paid if tax were apportioned on local revenue.

The two right-hand columns show the local assessed value of real estate, and the percentage of full value as estimated by the state board of equalization. The average percentage of full value for the entire State was estimated at 70+.

COUNTY	PREV. P. C.	NEW P. C.	AREA ACRES	POP. 1900	SPECIAL FRANCHISE ASSESSES	REAL ESTATE ASSESSES	EQUAL- IZED P. C.
Cayuga . .	.562	.454	415,629	66,000	\$588,320	\$31,719,000	.74
Jefferson . .	.561	.522	741,357	76,000	253,050	35,440,000	.83
Chautauqua .	.548	.595	656,538	88,000	987,220	37,403,000	.90
Ulster . .	.445	.565	663,331	88,422	290,690	26,293,827	.75
Chenango . .	.272	.205	548,035	36,500	127,000	14,756,889	.73
Greene . .	.220	.189	372,850	31,500	997,500	12,137,988	.72
Livingston .	.443	.181	384,300	37,000	120,690	23,752,499	.72
Clinton . .	.160	.213	591,168	47,000	78,135	6,302,627	.50
Essex . .	.171	.176	1,152,188	30,000	77,000	10,352,776	.79
Franklin . .	.186	.201	1,026,034	42,000	113,765	10,467,726	.74
Hamilton . .	.050	.070	1,086,683	5,000	52,500	3,588,356	.83
Lewis . .	.163	.115	778,147	27,000	34,260	9,197,452	.79
Putnam . .	.124	.077	129,417	13,000	26,830	8,249,346	.77
Schoharie . .	.187	.102	372,111	26,854	54,340	10,782,865	.78
Sullivan . .	.101	.138	603,897	32,000	71,000	5,822,178	.74
Warren . .	.130	.188	498,672	30,000	134,000	7,909,807	.80
Madison . .	.348	.265	374,334	40,000	130,825	17,990,160	.68
Washington .	.310	.248	495,632	45,000	226,000	17,115,170	.75
Herkimer . .	.357	.365	895,282	51,000	377,580	24,403,514	.90
Schenectady .	.360	.378	114,948	47,000	441,570	22,587,038	.70
Dutchess . .	.754	.549	477,493	81,670	538,700	41,052,423	.72
Orange . .	.726	.595	478,513	103,000	604,000	37,719,122	.68
Suffolk . .	.757	.408	480,392	77,000	472,785	48,924,485	.80
Niagara . .	.684	.709	294,527	75,000	1,100,000	44,619,834	.81

Statement showing percentage of state tax actually paid by each county of the State of New York in 1902, on the basis of equalized assessments, and percentage which each county would have been required to pay if the state tax had been apportioned on the basis of local expenditure or revenue.

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	PERCENTAGE PAID ON EQUALIZED ASSESSMENTS	PERCENTAGE IF APPORTIONED
Albany	1.517	1.486
Allegheny . . . . .	.252	.206
Broome . . . . .	.571	.495
Cattaraugus . . . . .	.404	.333
Cayuga . . . . .	.562	.454
-Chautauqua . . . . .	.548	.595-
Chemung . . . . .	.436	.397
Chenango . . . . .	.272	.205
-Clinton . . . . .	.160	.213-
Columbia . . . . .	.409	.328
Cortland . . . . .	.204	.168
Delaware . . . . .	.248	.237
Dutchess . . . . .	.754	.549
-Erie	5.246	6.120-
-Essex . . . . .	.171	.176-
-Franklin . . . . .	.186	.201-
Fulton . . . . .	.250	.246
Genesee . . . . .	.400	.185
Greene . . . . .	.220	.189
-Hamilton . . . . .	.050	.070-
-Herkimer . . . . .	.357	.365-
Jefferson . . . . .	.561	.522
Lewis . . . . .	.163	.115
Livingston . . . . .	.443	.181
Madison . . . . .	.348	.265
-Monroe	2.370	2.710-
Montgomery . . . . .	.431	.368
Nassau . . . . .	.745	.461
-New York City	66.431	68.107-
-Niagara . . . . .	.684	.709-
-Oneida . . . . .	.974	1.076-
Onondaga	1.803	1.796
Ontario . . . . .	.500	.287
Orange . . . . .	.726	.595
Orleans . . . . .	.259	.168
Oswego . . . . .	.457	.396
Otsego . . . . .	.359	.234
Putnam . . . . .	.124	.077
Rensselaer	1.224	1.064
-Rockland . . . . .	.252	.294-
St. Lawrence . . . . .	.567	.359
-Saratoga . . . . .	.440	.449-

	PERCENTAGE PAID ON EQUALIZED ASSESSMENTS	PERCENTAGE IF APPORTIONED
-Schenectady . . . . .	.360	.378-
Schoharie . . . . .	.187	.102
Schuyler . . . . .	.116	.071
Seneca . . . . .	.256	.153
Steuben . . . . .	.539	.428
Suffolk . . . . .	.757	.408
-Sullivan . . . . .	.101	.138-
Tioga . . . . .	.225	.171
Tompkins . . . . .	.274	.217
-Ulster . . . . .	.445	.565-
Warren . . . . .	.130	.188
Washington . . . . .	.310	.248
Wayne . . . . .	.440	.232
-Westchester	2.620	3.017-
Wyoming . . . . .	.251	.159
Yates . . . . .	.181	.084
	100.000	100.000

Counties checked would pay more.

SEPARATION OF THE SOURCES OF STATE AND LOCAL REVENUES AS A PROGRAM OF TAX REFORM

BY PROFESSOR T. S. ADAMS

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MUCH of what I shall have to say this afternoon is, unfortunately, critical or destructive, and because of that fact I desire to state emphatically, in the very forefront of my remarks, that I am in hearty sympathy with much and perhaps most of that which is now being done in the name of this reform. No one can deny that in the average State the device of state equalization has been a failure. No one can deny that some of the taxes now levied by the local governments belong more logically to the state government. No competent critic will question the statement that the reform movement which has brought practical separation in New York, Connecticut, Vermont, New Jersey, Oregon, Pennsylvania, Ohio, Wisconsin and other States, has been in the main a wholesome and logical development, worthy of being imitated in States which have not yet taken this first step. But when all this is said, the commonplace fact remains that the separation of state and local revenues, like other good things, is capable of being pushed too far; is capable of being interpreted in the wrong spirit; is capable — if we adopt it too blindly, too uncritically — of leading us off into a blind alley of mis-called "reform," in which true progress will be brought to a dead stop just when advance seems most certain. The object of this paper is to separate what I believe to be the true from what I believe to be the false, in this reform; to attempt to forecast the second and the third and the future stages generally, of that broad program of fiscal progress of which the separation of state and local revenues is the first step. For, it is important to note, the separation of state and local revenues has ceased to be merely an

end in itself, and has taken on added significance as the initial step of a thoroughgoing reform. "We are justified," says the recent Missouri Tax Commission, "in saying that this separation of the sources of state and local revenues is now generally recognized as the first essential step in any enduring tax reform."

The second step in the opinion of most writers and tax commissioners, who have recently considered this subject, is the so-called "Home Rule" or "Local Option." Separation, says the Report of the California Commission (of 1906) on Revenue and Taxation (p. 11), "establishes, at once, home rule in matters of local taxation." And so similarly the Report of the Missouri Commission of 1907 (p. 10): "The local taxing districts, the counties and cities of the State, will then (when separation is effected) have practical home rule in matters relating to taxation." And, "as regards the question of adequate local revenue, the simplest plan indeed," as Professor Seligman expresses it, "is to have a separation of state and local taxation, with local option on the part of the localities to tax or to exempt from taxation whatever classes of property they see fit."¹

From these expressions it would appear that the dual program of separation and home rule is one, primarily, of financial decentralization. The state government having taken over most of the fees and license taxes, nearly all of the corporation taxes, and perhaps some of the taxes on personal property, in addition, of course, to the inheritance tax, blandly says to the wondering little local governments gathered about the maternal knee: "Now children, you are free. Go your way and I shall go mine. I shall keep the taxes and revenues just mentioned, and you — you can have the general property tax. Considering the liberality of the division, I confidently expect you to be able, in the future, to get along without the pernicious and demoralizing tax on personal property."

This thorough divorcement of state and local revenue systems is, on the surface, exceedingly attractive to almost every one. The economist looks upon it with favor because it promises the abolition of the personal property tax. The single taxer applauds it, because it legalizes the exemption of improvements

¹ Seligman, *Political Science Quarterly*, Vol. XXII, pp. 312-313.

as well as that of personal property. The business man approves it because it offers a means of securing honorably and openly that exemption of plant and stock which so many merchants and manufacturers at the present time are securing illicitly and covertly. Of course, it may mean, instead of exemption, more strenuous attempts to assess personal property, and increasing efforts, in most localities, to lighten the load upon real estate by increasing the burden upon business. But the advocates of Home Rule are willing to take their chances. The program of reform apparently promises greater liberty to everybody concerned, and, as consistent Democrats, they properly refuse to be frightened by the fact that liberty may degenerate into license.

Despite its attractions, however, I believe that, on the whole, the program just described — the idea of complete separation of state and local finances with fiscal autonomy in each sphere — is impossible of realization and retrogressive in direction, making away from and not toward the real solution of our most important problems. I believe that real progress lies in the direction of centralization, not decentralization, of fiscal control. The reasons for this statement must be discussed in some detail.

I. In the first place separation and home rule cannot materially increase the positive fiscal freedom of the local governments. Generally speaking, they can be given the freedom to devise new exemptions, but not to levy new taxes. The constitutional amendment in Missouri, for instance, merely grants to the local divisions the right to exempt or reduce the tax rate upon certain classes of property. The local governments are given no power or discretion to experiment with substitutes for the personal property tax. Take the income tax, for example. Not only would it be impossible for a local government to administer the income tax without the right to call upon other officers of the State for information and assistance, but the difficult definitions and interpretations of income which the various local governments would introduce would bring about an intolerable amount of multiple taxation. Or take the much more feasible project of license or business taxes upon commercial and manufacturing concerns in lieu of the present taxes upon plant and stock. The various local

districts of a State could never be permitted to define and manipulate such taxes as they might see fit. Suppose a manufacturing concern had its factory and warehouse in Village A and its principal office and salesroom in City B. The village might impose the present property tax on plant and stock, while the city might — by adopting some plan of apportioning the total capital value of such concerns according to business done or gross income — tax practically all of this property again in another way. Furthermore, the local governments could not safely be permitted to tax individual categories of personal property as they saw fit. Take mortgage taxation. County A might institute a recording tax and County B the separate taxation of mortgages as personal property. Yet an individual mortgagee residing in B might lend his money in County A, with the result that, whether mortgagee or mortgagor ultimately paid the tax, it would be double or multiple taxation of the most vicious kind. In general, it is a safe conclusion that the income tax, business taxes and all manner of *ad valorem* assessment, in the spirit of the so-called unit rule, would have to be denied the local governments under the scheme of "Home Rule." With the growing practice of distributing the intangible values of going concerns in accordance with their business or tangible property, it is doubtful whether even the method of assessing tangible property can be left to the discretion of the local governments. The opportunities for double taxation are too manifold. While the habitation or occupancy tax might safely, perhaps, be left to the local governments (although even this is problematical), most of the possible substitutes for the personal property tax can only be introduced as state taxes. In other words the tax laws for the local districts will always have to be made by the state legislature.

Evidently, then, the phrase "Home Rule" does not mean exactly what the words imply. We want the local governments to have the liberty to exempt personal property, but we do not want them to have liberty to tax corporations as they please. We are advocating freedom when what we want, or at least the only thing we can have, is another kind of control. What we need is, not less state regulation in the matters of local taxation, but more intelligent state regulation.

II. Not only is centralization a good thing, but we are getting more centralization every day. If we examine the forward movement which has resulted in partial or complete separation in several of our most progressive commonwealths, we find that it was aimed primarily at the reform of corporation taxation, and achieved separation, incidentally, largely as a by-product. (Wisconsin, for instance, has ceased to levy property taxes for the support of the state government, but there has been no popular demand for separation in Wisconsin, practically no discussion of the subject and little attention paid to it.) Corporation taxation, under the old régime, when controlled by the local governments, had proved a striking failure; the assessment of such corporations had to be centralized, and in the process of centralization the State retained many corporation taxes simply because it was difficult to apportion corporate values, for purposes of taxation, among the various local districts. These corporation taxes proved so lucrative in many cases that it became practicable to discontinue the levy of state property taxes.

Now there is just one element common to this movement in practically all States. It is not the separation of state and local revenues. Many advanced States, Massachusetts, for instance, are not yet within striking distance of separation. Neither is it the complete retention of corporation taxes by the State. The one characteristic of the advance movement which is always and everywhere found is the centralization of the assessment power. The most striking characteristic of the past was the decentralization of the administrative machinery of taxation. The most striking feature of the two present is the universal and rapid progress towards the centralization of fiscal control. And this centralization is but an *incident* of the movement, which is really for *more efficient administration*. And the banner of reform is being carried by the State Tax Commission.

It is unnecessary to discuss in detail the evolution of the permanent tax commission. At the present time permanent commissions exist in at least nine States, and scarcely a year passes without the creation of a new commission. As the number of such commissions increases, their functions are

multiplied. At first they did little more than assess a few important classes of corporations. Gradually new duties, broader powers, were added; they were instructed to provide uniform blanks for local assessments, to assist or actually to make state equalizations, to inspect and criticise the work of local assessors, to revise county equalizations and order reassessments of property. To-day the tax commissions of seven States are empowered to institute proceedings for the removal of inefficient assessors; in seven States they are authorized to add property to the assessment rolls or to order the reassessment of particular parcels of property; in four States they may order the reassessment of entire districts; and in six States they are authorized to review and readjust county equalizations. It is no unwarranted stretch of the imagination to foresee a time when the whole machinery of local and state assessment, in the more advanced American commonwealth, will be coördinated and correlated under the control of a high-grade tax commission; when a permanent corps of expert assessors, holding office during good behavior and absolutely divorced from politics, will banish from American administration — and American politics — the miserably inefficient local assessor. It is because I see in the present program of Separation and home rule, the potential beginnings of a counter movement to this centralization of assessment, which seems to me so supremely important, that I take upon myself the unpleasant task of scrutinizing so critically the possibilities of a program with which, in the main, I am in hearty sympathy. If home rule, local option and fiscal decentralization militate in any important way against the reform of the local assessment work, they are not worth the cost.

III. The position just taken, the proposition that Separation should be judged according as it strengthens or weakens the character of the assessment work of the State, may be regarded as the central thesis of this paper, and the remainder of my time will be devoted to the consideration of a somewhat miscellaneous group of topics bearing upon this point.

First of all I desire to recall to your attention the very familiar and exceedingly important fact that, measured in

dollars and cents, the work of the local assessors is far and away the most important part of our fiscal system. Compared with the general property tax, corporation taxes, inheritance taxes and all the other taxes put together pale into insignificance. In 1902 more than three fourths of all the general revenues of the state and local governments came from taxes upon general property, and if the state taxes levied upon general property in that year had all been secured in some other way, — say, by subventions from the federal government, — even then two thirds of the aggregate general revenues of the state and local governments would have been raised by local taxes upon general property. Whether we keep or discard the taxation of personal property, the local assessor will, for many generations, continue to play the principal rôle in the work of state finance, and upon his probity and efficiency will depend the real success or failure of our fiscal system.

Now in recent years the statement has frequently been made that Separation itself, carrying with it the cessation of state taxation upon general property and the abolition of the state equalization, would prove the most effective means of improving the work of the local assessors. The Report of the California Commission on Revenue and Taxation is particularly enthusiastic on this point: "If there were no state tax to be apportioned among the counties, on the basis of local assessed valuation, there would be no object or inducement to the assessor or to the citizens of the county to obtain a low valuation. In fact, there would be more inducements to the assessor to assess the property as nearly as possible at its full market value in order to avoid inequalities between the citizens among his own constituents, and to protect himself against the charge of favoritism. The probability is, that in order to enjoy the advertising effect of a low tax rate, the great inclination would be for the assessor to raise the valuation rather than reduce it. A high tax rate is bad advertisement for a city or a county, and if there is no state tax to be imposed upon the same valuation, the county could have the advantage of the low rate by the simple process of raising the assessed valuation from its present level of about 50 per cent or 60 per cent to its full value." (pp. 62-63.)

With this interpretation of the probable effect of Separation I find myself wholly unable to agree. The influences or factors responsible for inefficient assessment work are so numerous that the desire to evade state taxes is really a negligible consideration. Enumerate these factors — first, the inherent difficulties of the task; next, the political atmosphere in which the assessor too often works; then, the insufficient time, insufficient pay, desire to evade county taxation, desire to favor personal friends and political associates — enumerate these factors, and it is plain, without reference to experience, that the mere discontinuance of state taxation of general property can work no appreciable improvement. If reference to experience is needed, I can only say that the practical Separation accomplished in Wisconsin has not, in the opinion of those best qualified to judge, exerted any appreciable influence upon the character of the assessment work. There is the same old struggle over the county equalization, the same old strife between city and county, the same old scramble of the individual taxpayer to get under the local assessment.

How could it be otherwise? Of the general property taxes — \$706,660,244 all — collected in this country in 1902, only \$83,320,134, or 11.6 per cent, went to the state governments, while \$624,340,110, or 88.4 per cent, went to the counties, cities and other local divisions. These figures furnish a good measure of the part which the desire to escape state taxes plays in demoralizing local assessors. The counties alone collected nearly 75 per cent more under the general property tax than the States. If the state governments should abandon the \$83,320,134 which they are now (or were in 1902) levying on general property, there would still remain \$624,340,110 to be distributed and equalized among the taxpayers of the local divisions. For the state government to abandon this greater task of equalization is a cowardly evasion of its chief duty.

Another current impression, which I believe to be similarly erroneous, is the idea that, if the personal property tax is abolished, the assessment of real estate will be on the whole equitable and satisfactory. "The local taxation of real estate," says the recent Special Tax Commission of the State of New York (p. 6), "is now on the whole free from any serious

objection." This may be true of New York, but it is certainly not true of most American States, and cannot become true so long as assessors are selected according to prevailing practices, and work under present conditions. During the past four years I have devoted a large part of my time to an intimate study of real estate assessments, in a State in which the quality of the assessment work is rather above than below the average. During that time I have compared, in the case of several hundred thousand parcels of real estate, the true value as determined by actual sale with assessed value as determined by the local assessors. The deliberate conviction, forced upon me by this examination, is that the real estate assessment is, on the whole, a marked failure from the standpoint of equality. In assessment districts in which the average ratio of assessed to true value is maintained consistently at 65 or 70 per cent, individual parcels will be assessed all the way from 20 to 120 per cent of true value. We talk glibly about the ease with which real estate can be assessed. The truth is that it is a task which challenges the highest skill of *bona fide* experts. Think of the speculative uncertainty of the value of farm lands adjoining city suburbs; the baffling variety of fixed plant and machinery ordinarily assessed as real property; the problem thrust upon the county assessor by the presence in some small village of one or two manufacturing plants of whose value only an expert of long experience in that particular industry can furnish any estimate; and I think you will agree with me that the problem of assessing real estate efficiently cannot be left to the local assessors, that it demands expert treatment which only the general government, by dealing with such problems in a wholesale way, can afford to provide.

Finally, I desire to call attention to the fact that Separation does not really abolish the state equalization nor prevent the distribution of the burden of state taxation among the various local divisions. What Separation actually does is to substitute for a conscious distribution of state burdens in accordance with the value of property, an unconscious, unseen and more or less haphazard distribution, which shifts the burden we know not where, avoids the evil of faulty equalization according to property by flying to other ills we know not of. Like the ostrich

in the thunderstorm, we stick our heads in the sand and stoutly maintain that it is not raining.

Consider the proposition a moment and it will cease to be merely fanciful. Ordinarily, Separation can only be realized by the State's retention of the more important corporation taxes. Some of the corporations involved, or more accurately some of the taxable corporate values involved, *e.g.* trust companies in New York, might with equal propriety, in whole or in part, be assigned to the local governments for taxation; and when they are not so assigned, such local divisions bear *pro tanto* the burden of supporting the State. And other things being equal, assignment to the local divisions should be the rule and not the exception. Unless there is no natural relation between property or business and the expenses of government, there is a *prima facie* presumption in favor of local taxation; and this initial presumption is indefinitely strengthened by the enormous fiscal burdens under which our municipalities are now staggering. For it is probably true — although I speak with hesitancy on this point — that Separation as it is ordinarily achieved considerably increases the burden of the city governments, in the sense that the cities would probably receive the major portions of such corporate values if they were localized according to the best principles of apportionment.

Many persons will commend Separation for this very reason, on the ground that the enormous escape of personalty in the cities makes the latter fit recipients of increased state taxation. But I believe this contention is unsound. It loses sight of the stupendous social tasks thrust upon our cities by the mere growth of population. City government, to a large extent, is characterized by what the economists call the law of increasing costs. And it loses sight of the still more important fact, that shifting a larger load of state taxes upon the city communities is not going to get the extra load on the shoulders of the men who evade the personal property tax. In short, it fails to improve the distribution of taxes between man and man in the city. And the typical city taxpayer is by no means a plutocrat. He is an exceedingly modest individual with a small encumbered piece of real estate for which he has been charged an exorbitant price. The city governments have

already as much as they can bear, without having their assessment rolls raided by the state government.

Moreover, it is not only corporation taxes which the state governments have monopolized. The largest source of state revenue in New York is the liquor license; there would be no difficulty in assigning that revenue to the appropriate local divisions. The second most productive source of state revenue in Pennsylvania is the tax or group of taxes on personal property. Are its burdens distributed among the local districts, and if so, is the distribution more or less equitable than that which would be accomplished by a conscious state equalization? In order to separate the sources of state and local revenue in California, the Commission on Revenue and Taxation of that State proposes that the central government shall retain, in addition to the poll, inheritance and insurance premium taxes, all taxes upon steam and street railways; express companies; car companies; light, heat and power companies; telegraph and telephone companies; the corporate excess of banks and all corporate franchises not covered by the above taxes. Unless the presence of property at a place has no connection with the public expenditures of that place, unless the right to exploit the commercial opportunities of a place creates no obligation to pay taxes at that place, unless the Adams Express Case is moonshine and the principle of the Ford Franchise Law a delusion, then street-car companies, heating and lighting plants, most banks and some telephone companies owe most of their fiscal allegiance to fairly well-defined local districts; and when these local districts are deprived by the State of the power of taxing such corporations, they are saddled with burdens of state taxation which belong elsewhere.¹ The unseen equalization involved in Separation is a very real phenomenon. Certain it is that no state legislature should decide to separate the sources of state and local revenues without clearly understanding that under any scheme the expenses

¹ The California plan is cited merely for illustrative purposes, and not with the idea of criticising the California Commission who know infinitely more about the needs of California than the writer. What is meant is, that under ordinary circumstances, in the opinion of the writer, such a division of revenues would be manifestly unjust.

of the state government must be distributed in some way among the various local divisions, nor without satisfying itself that the new distribution of state burdens proposed will be more equitable than the old.

IV. The practical conclusions which I would derive from the preceding discussion may be formulated in the following statements:

1. The state legislature should, in my opinion, without reference to the local divisions and without respect for impossible plans of local fiscal democracy, abolish the personal property tax and introduce a substitute therefor, if one can be devised.

2. If this is impracticable, they should sanction at once any scheme of limited local option which will permit particular districts to abolish that fiscal abomination, the personal property tax. No plan should be entertained, however, which will interfere with central supervision of assessments and central control over county equalizations.

3. Limited local option should be introduced without reference to the Separation of state and local revenues.

4. Similarly, the question of what sources of revenue should be retained by the State ought to be settled absolutely on its merits, without reference to home rule, by a careful study of tax jurisdictions and the connection between property or business and the expenses of local government. Doubtful points should be decided in favor of the local jurisdictions; and equitable apportionment should not be strained one inch in order merely to supply the State with revenue enough to get along without the levy of direct property taxes. If, after the apportionment of sources between state and local governments, the State has not sufficient special revenue to pay its expenses, let the deficit be raised by a state tax upon real estate, including in real estate the corporate and commercial values assigned to the local governments. The evils of an equalization based upon real estate are less than the evils of the unconscious, haphazard equalization involved in the retention by the State of a number of revenues which more logically belong to the local divisions.

5. Finally, I assert with some confidence, that if the equali-

zation is confined to real estate, and if it is made by an efficient tax commission which takes its work seriously, it is not a curse but a blessing. It can be made, in the first place, with all necessary accuracy, so accurately in fact that no fair-minded person after studying thoroughly the conditions of the problem will question its substantial accuracy as between county and county. It can be made without prohibitive expense; it is not necessary, as is sometimes asserted, to reassess every parcel of real estate in the commonwealth to get at the truth. And in gathering the data upon which to base its conclusions, the tax commission will obtain indispensable information concerning local assessment work, besides securing material absolutely necessary for the proper performance of the work of county equalization. The county equalizations are, in the aggregate, more important than the state equalization; but at the present time they are woefully inaccurate. The county officials who make these equalizations are, as a rule, destitute of reliable data upon which to base their apportionments, and, like the local assessors, they will never do their work efficiently until they are forced to do so by central supervision and state aid. Reform in these matters must come from without.

A NEW METHOD OF RAISING STATE REVENUE

By C. B. KEGLEY

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IN a conference in which are gathered together those who have achieved national and international reputation as authorities on the subject of state and local taxation, my feeling is that I should be here as a student and not for the purpose of addressing the Conference on so important a subject as "A New Method of Raising State Revenue." I advocate no new ideas of my own, and the method I will submit is not new to many of those assembled here. Indeed, if I mistake not, those who rightly may be considered the founders or originators of this method are here present, and this makes me feel very much as if I was engaged in carrying coals to Newcastle. All I claim, and all I believe those of the Pacific Northwest who have gone farthest in applying this new method of raising state revenue can claim, is that we are leading in the efforts to practically apply the theories others have worked out for us. The theory of this new method of raising state revenue was completely worked out when it was first brought to my notice, and it is only in the sense that I have done and am still engaged in doing pioneer work in the effort to secure its adoption in my own State, that I have any right to speak of it as new or to make an appeal for its consideration and indorsement by the Conference.

The new method I advocate for raising so much state revenue as may be needed over and above the amount obtained by the taxation of proper special subjects is that adopted in principle by the State of Oregon. The plan is to apportion the state tax among the several counties in proportion to the revenue raised by each for local purposes.

This principle, when properly carried out, would impose the burden of supporting the State in a much fairer manner than can ever be done by the attempt to assess all forms of property

in the same manner, and then impose a rate of taxation upon property thus assessed for state purposes. Oregon made the mistake of not carrying out the principle to its logical conclusion. The tax should be apportioned in proportion to the entire revenue raised by each county, and all the taxing districts within each county.

It is very easy to see that the more highly developed and more densely populated a county may be, the more money it needs for local purposes in proportion to its taxable values, and the greater is the power to pay taxes. The tax apportioned in this manner will shift from the poorer and remote rural counties the burden they now bear, and impose it on the more thickly settled and prosperous counties. This change would do away with the universal temptation to undervalue property in order to shift the state tax to other communities. This incentive to undervalue is one of the greatest evils tax officials have to contend with. It produces inequality and dissatisfaction, if not downright fraud.

The attempt to tax all kinds of property by the same rules has in all times, and in all countries, imposed heavier burdens upon rural districts than cities, and in a large degree has measured the tax to be paid by each citizen by the amount of his consumption, rather than by the opportunity he enjoys to acquire wealth under protection of the State. The new method is a perfect corrective of such evils.

When as the chief executive of the largest organization of farmers in the State, I first called the attention of the members of the Washington State Grange to the desirability of following the lead of our sister State of Oregon in having this new method adopted by our own State, I had to point out that the provision in our state constitution which requires the uniform assessment and taxation of all property in the State at an equal rate barred the way, and that progress in taxation was impossible so long as the constitution forbade all changes. It was necessary therefore to inaugurate a campaign having for its object the essential constitutional amendments.

Since that time progress has been made, not only in Washington, but in other States along these lines.

The State of Minnesota has ratified by popular vote an amend-

ment to the constitution so that the only restraint upon the power of the legislature is as follows:

"The power of taxation shall never be surrendered, suspended or contracted away. Taxes shall be uniform upon the same classes of subjects, and shall be levied and collected for public purposes."

The legislature of my own State has adopted an amendment to Art. VII of the constitution, to be submitted to the people at the general election in November, 1908, which is identical with the Minnesota amendment. The legislature of Missouri has this year adopted a joint resolution to submit to the people an amendment to the constitution of Missouri, which will permit the apportionment of so much revenue for state purposes as shall be required, in excess of that derived from special taxes, on the basis of local revenue or in such other manner as the legislature may prescribe. The amendment also provides that "the counties and cities of the State may subject to taxation, for local purposes, the real and personal property within their jurisdiction, and may exempt any class of property within such jurisdiction from taxation either wholly or by reduction of the rate of taxation thereon; provided that any taxation or exemption from taxation made in any county or city shall be uniform upon the same class of subjects within such territory."

An amendment to the constitution of Illinois similar to that of Minnesota was strongly urged before the legislature of Illinois, and a state tax commission has been appointed by the Governor of Ohio to consider the advisability of amending the constitution of that State.

All these are moves in the direction favorable to the adoption of the method of raising state revenues here advocated.

More and more it is being appreciated that methods of taxation have an immense effect upon the welfare of the people, and it is my hope and the hope of the farmers of Washington that this Conference will result in arousing such interest in the subject that not only our own State, but every State in the Union, will soon have the most perfect state and local tax laws that can be devised.

TAXATION BY THE STATE OF PENNSYLVANIA

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I. TAX ON CAPITAL STOCK OF CORPORATIONS AND INTERESTS IN LIMITED PARTNERSHIPS, AND JOINT STOCK ASSOCIATIONS

THE largest single source of the revenue of Pennsylvania is the tax on the capital stock of corporations and interests in limited partnerships, and joint stock associations.¹ There is exempted from the payment of this tax so much of the capital stock of corporations, incorporated "for the purpose of erecting and maintaining a bourse or exchange hall or as a meeting place for merchants or other business men or for the exhibition of manufactured articles or natural products" or incorporated for "the purchase or sale of real estate or for holding, leasing and selling real estate," as is represented in a bourse, hall or exchange, unless a dividend is declared on the entire capital stock, or unless such real estate is sold, transferred, let or leased without notifying the secretary of the commonwealth. In the first of which cases the entire capital stock would be liable to the tax for the year in which the dividend was paid; in the latter case the entire capital stock would thereafter be subject to taxation.²

A second exception is expressly made for banks, savings institutions and foreign insurance companies, because they are otherwise taxed.

Another and a more important exception is made for that part of the capital stock "invested in and actually and exclusively employed in carrying on manufacturing within the State."³ The statute expressly states that there is not excepted from the tax that part of the capital stock of manufacturing

¹ Act of June 8, 1893, P. L. 353.

² Act of June 10, 1893, P. L. 417.

³ Act of June 8, 1893, P. L. 353.

companies invested for purposes not strictly incidental or appurtenant to its manufacturing business. So also is the tax collected from those corporations, limited partnerships and joint stock associations that "enjoy and exercise the right of eminent domain," even though they be manufacturing companies.

The rate of taxation is "five mills upon each dollar of the actual value of its whole capital stock of all kinds."¹ Fire and marine insurance companies, however, pay at the rate of three mills on each dollar.² Upon all "full paid, prepaid and fully matured or partly matured stock in any building and loan association" upon which cash dividends or interest are paid there is collected a tax of four mills on the dollar.³ So also there is a tax of ten mills upon every dollar of capital stock of "companies organized and incorporated for the purpose of distilling liquors and selling the same at wholesale,"⁴ while the other manufacturing "companies engaged in the brewing or distilling of spirits or malt liquors" do not enjoy the exemption of manufacturing companies but are subject to the regular tax of five mills.⁵

The tax upon the capital stock is in reality a "tax upon its property and assets."⁶ Or, as is said in Fox's appeal, 112 Pa. 354: "The capital stock is nothing; a myth; a mere name, excepting in so far as it is represented by investments made with the money paid into the treasury of the corporation on account of such capital stock. Hence it is clear that the courts have long since declared that a tax upon the capital stock of a corporation is a tax upon the assets and property of such corporation." So this tax is but a tax on realty and personalty owned by corporations, limited partnerships or joint stock associations. This view of the tax is important, for it has been held that that proportion of the capital stock of a company as is represented by real estate situated, or by personal property of a corporeal nature ordinarily kept, in another State is not subject to this tax.⁷ So also, although under the words of the statute, the tax is imposed upon the capital stock of all companies incor-

¹ Act of June 8, 1893, P. L. 353. ² *Ibid.* ³ Act of June 22, 1897, P. L. 178.

⁴ Act of July 15, 1897, P. L. 292.

⁵ Act of June 8, 1893, P. L. 353.

⁶ *Com. vs. Standard Oil Co.*, 101 Pa. 119.

⁷ *Com. vs. American Dredging Co.*, 122 Pa. 386.

porated or organized by or under the laws of any other sovereignty "doing business in . . . or having capital or property employed or used within this commonwealth,"¹ yet the tax is not imposed upon all the capital stock, but only on that portion which represents property within the State.² And if such property of a foreign corporation is invested in and actually and exclusively employed in carrying on manufacturing, of course within the State, it is exempted from taxation under the general provisions of the Act of 1893.³ But the property of neither domestic nor foreign manufacturing companies which is not so actually and exclusively employed is not exempted.⁴

While real estate situated and corporeal personal property ordinarily kept in another State is not subject to this tax, in accordance with the general rule of taxing personalty at the domicile of the owner, such property of a domestic corporation as has not acquired a situs in another jurisdiction is taxed in Pennsylvania.⁵ So also are included in the valuation mortgages on property in other States held by a domestic corporation.⁶ Another exception is made in the case of the stock of national banks, for under the federal statutes⁷ they are taxed by the jurisdiction within which the bank is situated.

A possible conflict with the power of the federal government over interstate commerce arose with the efforts of the state authorities to collect from the Pullman Palace Car Company a tax upon such proportion of the capital stock of the company as the number of miles over which it ran cars within the State bore to the whole number of miles in that and other States over which its cars were run. The United States Supreme Court held that inasmuch as about one hundred cars were continuously employed by the defendant corporation within the State,

¹ June 8, 1891, P. L. 229.

² *Com. vs. Standard Oil Co.*, 101 Pa. 119, and numerous cases following this decision.

³ *Com. vs. American Car and Foundry Co.*, 5 Dauphin Co. 111.

⁴ *Com. vs. Conglomerate Mining Co.*, 1 Dauphin Co. 85; *Missouri Furnace Co. vs. Cochran*, 12 P. L. J. (N. S.) 238; *Com. vs. Juniata Coke Co.* 157 Pa. 507; *Com. vs. Savage Fire Brick Co.*, 157 Pa. 512; *Com. vs. National Oil Co., Ltd.*, 157 Pa. 516; *Com. vs. East Bangor Consolidated Slate Co.*, 162 Pa. 599. As to investments in laborers' dwelling houses, see *Com. vs. Westinghouse Air Brake Co.*, 151 Pa. 276; *Com. vs. Savage Fire Brick Co.*, 157 Pa. 512.

⁵ *Com. vs. Pennsylvania Coal Co.*, 197 Pa. 551; *Com. vs. American Dredging Co.*, 122 Pa. 386. ⁶ *Com. vs. Pennsylvania Coal Co.*, 197 Pa. 551. ⁷ R. S. 5219.

although the individual cars were crossing and recrossing the boundary of the State, the State had the right to tax this property and that the method of assessment was just and equitable.¹

In accordance with the principle enunciated in *McCulloch vs. Maryland*² there is exempted from the state tax such portion of the property as is represented by the mail service, by the property of national banks (except so far as expressly allowed) or by a federal franchise. So, also, is the incorporeal patent right or copyright and corporate property invested in such right,³ but this exemption does not extend to the products manufactured under and by virtue of such right.⁴

Another matter connected with some difficulty was the imposition of this form of tax upon limited partnerships and joint stock associations which, in the common acceptance of the term, have no capital stock. The proviso to the first section of the Act of June 8, 1893,⁵ enacted "that for the purposes of this act interests in limited partnerships or joint stock associations shall be deemed to be capital stock and taxable accordingly." After the passage of the Act of May 9, 1899,⁶ and its amendment of May 8, 1901,⁷ providing for the creation of limited partnerships it became necessary to decide that companies created under those acts became subject to the provisions of the acts imposing the tax on capital stock and it was so decided by the attorney-general.⁸

The valuation of the capital stock is an important matter and the source of much litigation. The Act of June 8, 1891,⁹ makes it obligatory for the officers of every company subject to the tax to make a report in writing to the auditor general of certain specified facts and also to "estimate and appraise the capital stock of the company at its actual value in cash, not less, however, than the average price which said stock sold for during the year and not less than the price or value indicated or measured by net earnings or by the amount of profit made, and either declared in dividends or carried into surplus or sinking fund."

¹ *Pullman Palace Car Co. vs. Pennsylvania*, 141 U. S. 18.

² 4 Wheat 316.

³ *Com. vs. Philadelphia Co.*, 157 Pa. 527.

⁴ *Com. vs. C. D. & P. Tel. Co.*, 147 Pa. 121; 28 W. N. C. 515.

⁵ P. L. 353.

⁶ P. L. 261.

⁷ P. L. 149.

⁸ Opinion of Attorney-General Carson, Oct. 30, 1903.

⁹ P. L. 229.

And it is further provided "that if the auditor general or state treasurer, or either of them, is not satisfied with the appraisal and valuation so made and returned, they are thereby authorized and empowered to make a valuation thereof based upon the facts contained in the report herein required, or upon any information within their possession or that shall come into their possession and to settle an account on the valuation so made by them for the taxes, penalties and interest due the Commonwealth thereon," with the right of appeal to the courts reserved to the company.

From our previous discussion we know that the cash value of the property represented by the capital stock rather than the value of the shares of stock shall be appraised and this is so despite the fact that the report as required does not include a statement of the amount and value of the property and assets. But the appraisal shall not be less than the average price the stock sold for during the year. It has been held that it is not unjust to determine this value by adding the amounts received during the year at the sale of every share sold and dividing the sum by the number of shares sold.¹ Of course the appraisal may be more than such average price.² Inasmuch as it is required that the appraisal by the officers of the company must be made within the dates of November first and fifteenth, it has been argued, but unsuccessfully, that the selling price of the stock within such dates was the sole test of the value of the capital stock. It has been held that such price may be the test,³ but it is not the only test.⁴

Nor by the terms of the statute shall the appraisal be less than the "price or value indicated or measured by net earnings or by the amount of profits made and either declared in dividends or carried into surplus or sinking fund." It was early held that the words "net earnings" and "amount of profits made" were synonymous.⁵ In construing this minimum limitation so as to avoid injustice to such companies as have a large income from

¹ *Com. vs. People's Traction Co. of Philadelphia*, 183 Pa. 1405.

² *Com. vs. P. R. R. Co.*, 94 Pa. 474.

³ *P. R. R. vs. Com.*, 94 Pa. 474.

⁴ *Com. vs. P. R. R. Co.*, 145 Pa. 74; *Com. vs. Philadelphia Co.*, 3 Dauphin Co. 259; *Com. vs. Lehigh Valley R. R. Co.*, 37 Leg. Int. 407.

⁵ *Com. vs. Edgerton Coal Co.*, 164 Pa. 284.

a source about exhausted and to such companies whose earnings result from the consumption of the property or are used in the payment of interest on its debt, it became necessary to hold that net earnings or profits declared in dividends or carried into surplus or sinking fund were not the sole indication.¹ So while in these cases probable depreciation is considered, it would seem that no case clearly holds that probable future prosperity should be made of importance. But on the other hand the distribution of net earnings in the form of a stock dividend is considered, and its value is not fixed at the price for which it was distributed, but at the actual value of the dividend as ascertained.² So, also, earnings expended for extension and improvements are considered part of the net earnings.³

The actual value is purely a question of fact to be determined not from a consideration of one element, but from a consideration of many elements. The previous acts imposing a tax on the capital stock provided for its assessment "on the basis of the rate per cent of dividends when the dividend during the tax year equaled or exceeded 6 per cent; and when no dividends were made, on an appraisement of the capital stock; and when the dividend was less than 6 per cent, under some of the acts, the tax was assessed on the basis of the rate per cent of the dividend, and under others, on the assessed value of the stock."⁴ In the enforcement of the present act immediately after its passage the auditor general construed the act to lay down a hard and fast rule that the capital stock must be appraised at not less than a principal sum, 6 per cent of which would equal the net earnings of the corporation for the tax year. This construction was overruled in *Com. vs. Edgerton Coal Co.*, 164 Pa. 284.

Under the present rulings there is considered, of course, the value of the realty and of the tangible personal property.⁵

¹ *Com. vs. Edgerton Coal Co.*, 164 Pa. 284; *Com. vs. Jamestown & Franklin R. R. Co.*, 3 Dauphin Co. 255; *Com. vs. West End Coal Co.*, 182 Pa. 353; *Com. vs. Delaware, Lackawanna & Western R. R. Co.*, 3 Dauphin Co. 266; *Com. vs. Philadelphia Co.*, 3 Dauphin Co. 259; *Com. vs. Pittsburgh & Western R. R. Co.*, 166 Pa. 453.

² *Com. vs. People's Traction Co. of Philadelphia*, 183 Pa. 405.

³ *Com. vs. Minersville Water Co.*, 4 Dauphin Co. 170.

⁴ Whitworth, "Taxation of Corporations in Pennsylvania for State Purposes."

⁵ *Com. vs. N. Y., Pa., and Ohio R. R. Co.*, 188 Pa. 169.

The value of the franchise and privileges¹ are often of great importance as is the good will² and the value of an existing lease.³ A general element of importance is the earning capacity.⁴

The presumption against a legislative intent to impose a system of double taxation applies to that part of the capital stock invested in the shares of another corporation. Also as the personal property tax Act of June 8, 1891,⁵ provides that shares of stock in the hands of a holder are taxable, "except shares of stock . . . liable to the capital stock tax . . . or relieved from the payment of the tax on capital stock . . .," the exemption of such part of the property from the tax on capital stock has been established.⁶ But the same result was not reached when the corporations attempted to lessen their taxes by having their incumbrances deducted from the valuation of their property,⁷ and yet the incumbrances may be considered, for the interest on them is a fixed charge, and that they may "seriously depreciate the actual value of the property cannot be questioned."

In the case of transportation companies the value is reached by appraising the entire line and determining by the mileage basis the proportion that is subject to taxation in Pennsylvania.⁸ This method meets with the approval of the United States Supreme Court.⁹

II. TAX ON LOANS OR INDEBTEDNESS OF PRIVATE CORPORATIONS¹⁰

From the point of view of revenue to the state government the second most important tax is the tax on loans or indebtedness

¹ *Com. vs. L. S. & M. S. R. R. Co.*, 3 Dauphin Co. 172, is a clear precedent among many others. ² *Com. vs. John Haney Co., Ltd.*, 1 Dauphin Co. 178.

³ *Com. vs. Union Traction Co. of Philadelphia*, 1 Dauphin Co. 178.

⁴ *Com. vs. Allegheny Heating Co.*, 2 Dauphin Co. 91; *Com. vs. Delaware, Susquehanna & Schuylkill R. R. Co.*, 165 Pa. 44; *Com. vs. Prudent Life and Trust Co.*, 3 Dauphin Co. 264. ⁵ P. L. 229. ⁶ *Com. vs. Fall Brook Coal Co.*, 156 Pa. 488.

⁷ *Com. vs. N. Y., Pa., and Ohio R. R. Co.*, 188 Pa. 169; *Com. vs. Ontario, Carbondale, and Scranton R.R. Co.*, 188 Pa. 205.

⁸ *Com. vs. Western Union Telegraph Co.*, 2 Dauphin Co. 40, is a precedent among many others.

⁹ *Pittsburg, Cincinnati, Chicago & St. Louis R. R. Co. vs. Backus*, 154 U. S. 421.

¹⁰ An article describing this state tax and the tax on personal property by Roswell C. McCrea appeared in the *Quarterly Journal of Economics* for November, 1906. This article may perhaps have made a description of these two taxes unnecessary except for sake of completeness.

of private corporations. This tax is collected under the Acts of June 30, 1885,¹ and of June 8, 1891.² There were earlier attempts to single out this form of property for the purpose of collecting the tax through the corporate officers, but they failed by being construed as unconstitutional. For the first year little revenue was derived from this tax, for it was attacked on several grounds, but it has been to date upheld.

The acts provide that the treasurer of a corporation, when paying the interest on any "scrip, bond or certificate of indebtedness," shall deduct from such payments four mills on every dollar of the nominal value of the debt and return the same into the state treasury.

In the construction of this act by the courts it has been materially affected. The Pennsylvania courts decided that the indebtedness was taxable in Pennsylvania irrespective of the domicile of the holders.³ But the federal court overruled the state court,⁴ for it is held that this tax "is not a tax laid on the company nor on the bondholders as a body, but upon each resident bondholder as an individual,"⁵ and so differs from a tax on a mortgage interest in property. It will be noted that the act futilely but expressly provides that the tax be also imposed upon foreign corporations "doing business in this Commonwealth," for the United States Supreme Court has held that Pennsylvania could not require the officials of a foreign corporation paying the interest by check outside of Pennsylvania to deduct the tax.⁶

If no interest be paid, no tax is paid. If new bonds are issued for the interest, no tax is imposed unless the corporation be solvent.⁷

When unusual financial methods are resorted to, each case stands on its own merits as to whether or not the method stands on the same footing as a payment of the interest on money.⁸

The tax is collected by the treasurer or an agent of the cor-

¹ P. L. 193. ² P. L. 229. ³ *Com. vs. Susquehanna Coal Co.*, 72 Pa. 72.

⁴ *State Tax on Foreign-held Bonds*, 15 Wall. 300.

⁵ *Com. vs. P. R. R. Co.*, 150 Pa. 312.

⁶ *Com. vs. N. Y., L. E., and Western R. R. Co.*, 153 U. S. 628.

⁷ *Com. vs. P. R. R. Co.*, 150 Pa. 312.

⁸ *Com. vs. P. and R. C. and I. Co.*, 137 Pa. 481; *Com. vs. Union Traction Co.*, 192 Pa. 507.

poration, for which he is allowed 5 per cent commission when the sum paid into the treasury does not exceed \$1000; when it exceeds that sum but does not exceed \$2000, 1 per cent for the excess over \$1000, and on all beyond \$2000 one half of 1 per cent.¹

As we have seen that the tax is imposed or not according as the indebtedness is held by residents of Pennsylvania, or not so held, it is important for administrative purposes to know how the indebtedness is held. The corporate treasurers are in a position to know. If they willfully neglect the duty of ascertaining the facts as to this matter, the penalty falls on the corporation, for the state authorities presume that the bonds are held by residents.² But if the officers have exercised due diligence in the matter, this inference against the corporation is not drawn.³

The corporate loans so taxed are relieved from the payment of any other tax. The Act of June 10, 1885, provided that "the bonds, certificates or other evidences of indebtedness issued by it shall be exempt from all other taxation in the hands of the holders of the same." And the Personal Property Tax Act of June 1, 1889,⁴ enacted that no return should be made of the "obligations of public or private corporations, the tax upon which is required by law to be collected from the holder of such obligations, and paid into the state treasury by the corporation."

There are relieved from this tax on corporate indebtedness, as we have already noted, the indebtedness of foreign corporations, foreign held bonds of domestic corporations and bonds on which no interest is paid. In addition such loans as are held by other corporations in their own right are exempted because they are included in the valuation of the property for purposes of the capital stock tax,⁵ and also in accordance with the provision in the Act of June 8, 1893,⁶ "corporations, limited partnerships and joint stock associations liable to tax on capital stock under this section shall not be required to make any report or pay any further tax on the mortgages, bonds and other securities owned

¹ Act of April 15, 1834, P. L. 544.

² *Com. vs. People's Pass. R. R. Co.*, 183 Pa. 353; *Com. vs. Penna. Salt Mfg. Co.*, 145 Pa. 53. ³ *Com. vs. Lehigh Valley R. R. Co.*, 186 Pa. 235. ⁴ P. L. 420.

⁵ *Com. vs. Penna. Coal Co.*, 3 Dauphin Co. 142; *Fidelity Co. vs. Laughlin*, 139 Pa. 612; *Com. vs. Western Union Tel. Co.*, 2 Dauphin Co. 40. ⁶ P. L. 353.

by them in their own right," but the tax is paid on securities by the issuing corporation if such companies hold them in any other manner than in their own right.¹ The holdings of national banks are exempted from this tax on such holders of corporate indebtedness, for this is not a tax expressly allowed by act of Congress.² While bank notes, or notes discounted or negotiated by any bank or banking institution, savings institution, or trust company," are exempted,³ this exemption does not apply to bonds of another corporation.⁴ But corporate loans held by institutions of purely public charity or religion are exempted.⁵

It is finally important to remember that upwards of 75 per cent of the mortgages made to secure the payment of corporate bonds or other indebtedness contains a covenant providing that the interest or coupon shall be paid to the owner or holder "free and clear of all state taxes."⁶ Although it is often said that corporate indebtedness differs from private mortgage indebtedness, it may be that the difference is not distinguishing, particularly where a State has a tax of the nature of the capital stock tax of Pennsylvania, which is a tax on the entire corporate property, incorporeal as well as corporeal, and in the valuation of which the incumbrances are not deducted. It may be wise to also mention here that by stopping at the source the tax on corporate loans, it of necessity from administrative considerations discriminates between that wealth invested in interest-bearing loans and that invested in loans on which no interest is paid, by attempting to subject the latter class of loans to the problematical drag-net of the local assessors.

III. TAX ON MUNICIPAL AND COUNTY LOANS

The tax on loans of municipalities, counties, boroughs and incorporated districts⁷ is very similar to the tax on loans of

¹ P. L. 353.

² R. S. 5219; *Boyer vs. Boyer*, 16 W. N. C. 1.

³ Act of June 8, 1891, P. L. 229.

⁴ *Wilkes Barre, D., and S. B. vs. Wilkes Barre*, 148 Pa. 601.

⁵ *Mattern vs. Canevin*, 213 Pa. 588.

⁶ "Compendium and Brief History of Taxation in Pennsylvania," 1906. Published by the Department of the Auditor General.

⁷ Act of April 29, 1844; P. L. 486, Section 42; Act of April 30, 1864; P. L. 219, Section 4; Act of June 8, 1891; P. L. 231.

private corporations in its method of collection and in its economic function and burden except that the public corporations do not covenant to pay any state taxes although they may as a matter of fact bear their burden. The rate of the tax is four mills upon the nominal value of the indebtedness.

By special acts there are exempted bonds issued by boroughs and cities in payment of subscription to the stock of railroads, and bounty and defense bonds.¹ Bonds issued by cities, but subsequently purchased by the commissioners of the sinking fund and held by them, are not liable to taxation,² nor are those which are overdue, outstanding and redeemed.³ So also is exempted such county loans as are "owned by any public corporation within such county, and the income of which is by law appropriated to the support of the poor, and the maintenance of the public roads of such county."⁴

Many of the principles discussed under the tax on loans of private corporations are applicable to the loans of public corporations.

IV. TAX ON STOCK OF BUILDING AND LOAN ASSOCIATIONS

A tax very similar in its nature and in its method of collection to the tax on corporate loans, but of little importance, is the tax upon full paid, prepaid and fully matured or partly matured stock in any domestic building and loan association or in any foreign association doing business within Pennsylvania and upon which cash dividends or interest are paid. There is exempted the unmatured stock in process of payment and such unmatured stock upon which periodical payments are required to be made which seems to contradict any tax upon partly matured stock. The rate of taxation is "equal to that required to be paid upon money at interest by the general tax laws of this State," that likely is four mills upon the value of the stock. The collection is made by the auditor general's department, the domestic associations making a report to him directly, and the foreign associations reporting through the banking depart-

¹ Whitworth, "Taxation of Corporations," p. 209.

² *Com. vs. Pittsburg*, 1 Dauphin Co. 287.

³ *Com. vs. Allegheny City*, 15 W. N. C. 316.

⁴ Act of March 24, 1877, P. L. 44.

ment.¹ Many possible questions have as yet not been decided, and as a source of revenue the tax is unimportant, fifty-three associations paying in 1905, \$12,371.04. I will not discuss it further except to note that it has been decided that any kind of stock paying interest is subject to the tax,² and that these associations are relieved from the state personal property tax, as we shall see later, and also to repeat that they are exempted from the capital stock tax.

V. TAX ON SHARES OF STOCK OF BANKS AND SAVINGS INSTITUTIONS

After many acts subjecting banks to taxation had been tried, the tax is at present collected under the Act of July 15, 1897.³ The tax is imposed on every bank or savings institution incorporated either by the State or by the national government, having capital stock at the rate of four mills upon each dollar "of the actual value" of the stock "ascertained and fixed by adding together the amount of capital stock paid in, the surplus and undivided profits, and dividing this amount by the number of shares." The bank or institution has a choice of being subject to this tax or of paying "a tax of ten mills on the dollar upon the par value of all shares of said bank that have been subscribed for or issued," and of thereby relieving "the shares . . . and so much of the capital and profits of such bank or savings institution, as shall not be invested in real estate . . . from local taxation. . . ." This exemption has been so construed that the holders of the shares are not thereby relieved from the state personal property tax,⁴ except in the case of shares of national banks which cannot be taxed in the hands of the holders.⁵

The act also provides that in case the bank or institution "shall collect annually from the shareholders thereof said tax . . . and pay the same into the state treasury on or before the first day of March in each year, the shares and so much of the capital and profits of such bank or savings institution as shall not be invested in real estate shall be exempt from local taxa-

¹ Act of June 22, 1897; P. L. 178.

² Opinion of Deputy Attorney General Flietz, April 27, 1899. ³ P. L. 292.

⁴ *Commissioners vs. Merchants & M. National Bank*, 168 Pa. 309; *Com. vs. County of McKean*, 200 Pa. 383.

⁵ *Boyer vs. Boyer*, 113 U. S. 689.

tion under the laws of this Commonwealth; and such bank or savings institution shall not be required to make any report to the local assessor or county commissioners of its personal property owned by it in its own right for purposes of taxation, and shall not be required to pay any tax thereon." If this option is exercised, it would appear that the exemption did not extend to the tax on corporate loans,¹ but as a matter of fact no such tax is paid.

VI. TAX ON GROSS RECEIPTS OF BANKERS AND BROKERS AND TAX ON NET EARNINGS OR INCOME

It may be well to mention at this point the tax of 1 per cent on all receipts arising from the year's business of stock brokers, bill brokers, exchange brokers, merchandise brokers and private bankers,² and also there may be noted here the tax of 3 per cent on the net earnings or income received during the year by every incorporated company or limited partnership except those subject to the capital stock tax, insurance companies, incorporated banks and savings institutions having capital stock, and corporations and limited partnerships chartered or organized for manufacturing purposes. Therefore, it appears that this tax falls on unincorporated banks and savings institutions. And it is well to observe that the payment of this tax is "in addition to any taxes on personal property to which the company may be subject."³

Both these taxes are taxes on the franchise or privilege,⁴ and therefore it is immaterial in what form of wealth their capital is invested.⁵ In order to determine the amount of tax on net earnings due, it is held that "net earnings are the excess of gross earnings over expenditures defrayed in producing them."⁶ Therefore, there are not deducted earnings applied to the payment of the capital stock⁷ nor losses on securities,⁸ but the losses and interest paid on money to carry on the business of banker and broker is considered.⁹

¹ Opinion of Auditor General Mylin, Dec. 21, 1897.

² Act of June 13, 1901, P. L. 559; Act of June 27, 1895, P. L. 396.

Act of June 7, 1879, P. L. 112; Act of June 1, 1889, P. L. 420.

Philadelphia Contributionship, etc., *vs.* Com., 98 Pa. 48.

³ Com. *vs.* McKean, 3 Dauphin Co. 147.

⁴ Com. *vs.* P. & E. R. R. Co., 164 Pa. 260. ⁷ Com. *vs.* Ocean Oil Co., 59 Pa. 61.

⁸ Philadelphia *vs.* Com., 98 Pa. 48. ⁹ Com. *vs.* Weiser & Son, 1 Pearson 343.

June 8, 1891,¹ three fourths of the amount collected is returned to the county or city collecting the tax. Various reasons for this action are assigned, but it would seem that the legislature stated its reasons in saying that the consideration for so returning the tax were that "no claim shall be made upon or allowed by the Commonwealth for abatements, tax collectors' commissions, extraordinary expenses, uncollectible taxes, or for keeping a record of judgments and mortgages."

The tax is collected under the provisions of the Acts of June 1, 1889,² and of June 8, 1891.³ The tax is required from any owner or holder of the property taxed at the rate of four mills on each dollar of the value thereof. The subjects of the tax are:

"All mortgages.

"All moneys owing by solvent debtors, whether by promissory note, or penal or single bill, bond or judgment.

"All articles of agreement and accounts bearing interest.

"All public loans whatsoever, except those issued by this commonwealth or the United States.

"All loans issued by or shares of stock in any bank, corporation, association, company or limited partnership, created or formed under the laws of the Commonwealth or of the United States, or of any other State or government, including car trust securities and loans secured by bonds or any other form of certificate or evidence of indebtedness, whether the interest be included in the principal of the obligation or payable by the terms thereof.

"All moneys loaned or invested in other States and Territories, the District of Columbia, or foreign countries.

"All other moneyed capital in hands of individual citizens of the Commonwealth.

"All stages, omnibuses, hacks, cabs and other vehicles used for transporting passengers for hire, except steam and street passenger railway cars, owned, used or possessed within this commonwealth by any person or persons, or by any corporate body or bodies.

"All annuities yielding annually over \$200."

There are by the legislature expressly excepted from taxation under this act:

Accounts not bearing interest.

Shares of stock in any corporation or limited partnership liable to the capital stock tax or relieved from the payment of tax on capital stock.

¹ P. L. 233. ² P. L. 420. ³ P. L. 229.

Obligations of public or private corporations, the tax upon which is required by law to be collected from the holder of such obligations, and paid into the state treasury by the corporation.

Loans issued by this commonwealth or the United States.

Bank notes or notes discounted or negotiated by any bank or savings institution or trust company.

Building and loan associations.

So also is exempted as we have seen:

"Mortgages, bonds and other securities owned in their own right by such corporations, etc., as pay the capital stock tax. If they are manufacturing corporations they are in practice taxed, but may be, at least in part, exempt at law."¹

"Banks paying the tax on bank stock on or before March the first.

"Loans held by charitable and religious institutions."²

Property which is not enumerated is likely exempt despite the inclusion of other "moneyed capital in the hands of the individual citizens" of such States.

While corporate loans on which taxes are paid by the corporation are relieved from this tax, we have seen that no taxes are paid on such loans on which no interest is paid. Accordingly this latter class is subject to the tax,³ but it is collected to only a slight extent, because the tax payment by the corporation is made at the end of the year, while the holder of the obligation makes his return at the beginning of the year, when he does not know whether or not interest will be paid.

In the case of the stocks and bonds of foreign corporations held by residents of Pennsylvania, it should be observed that they are subject to taxation within Pennsylvania⁴ unless they pay the capital stock tax. So also in the case of money at interest—it is taxed at the domicile of the owner rather than at the place where the money is at interest.⁵ But as we have seen in the consideration of the tax on corporate loans, the obligations of domestic corporations held by non-residents are not liable to a tax of this character.

¹ Act of June 8, 1893, P. L. 353; Eastman, "Taxation for State Purposes in Pennsylvania," p. 64.

² *Mattern vs. Canevin*, 213 Pa. 588. ³ *Perry Co. vs. Trautman*, 144 Pa. 361.

⁴ *McKean vs. County of Northampton*, 13 Wright 519.

⁵ *Dauphin Co. vs. Banks*, 1 Pears 40.

The machinery for the collection of a tax is important, and it is particularly so in a tax of this character. Taxables are furnished with blanks which, when filled out, are sworn to. Assessors add to these statements such property as they know has been omitted, and if the taxable has made no return, the assessors supply the deficiency after ten days' notice. The returns of the assessors are revised by the county commissioners and boards of revision of taxes.

A statement of these returns is sent by the local officers to the State Board of Revenue Commissioners, composed of the auditor general, state treasurer and secretary of the commonwealth. This board is to determine the value of property made taxable by law, adjusting and equalizing the same, so as to make all taxes bear equally upon all property subject to taxation for state purposes in proportion to its actual value. They are to assign to each city or county the value of taxable personal property therein and the quota of tax to be raised therefrom.

The tax is collected by the city and county authorities. The respective treasurers retain a commission of one per centum on the amount of tax paid into the state treasury when they make their payments.

In order to collect the tax more thoroughly on mortgages, articles of agreement to secure the payment of money, judgments and other instruments to secure debts, daily records are kept by the recording officers and reports are made monthly to the county commissioners or board for revision of taxes as the case may be. From these reports the last-named officials prepare for the assessors' use records showing such of these evidences of debts as are subject to the tax.

It has also been enacted that it shall be unlawful for lenders to require borrowers to pay the tax, and if the lender has paid the tax, it shall be deemed to be usury and be subject to the laws governing the same.

XI. TAX ON COLLATERAL INHERITANCES

This tax is the source of a not inconsiderable amount of revenue and is of great interest to the practicing attorney. But the considerations surrounding the imposition of this tax are peculiar to itself, and so I pass it by with scant notice. There is a

tax of "five dollars on every hundred dollars of the clear value of all estates passing by will or under the intestate laws of this State to any other than father, mother, husband, wife, children and lineal descendants born in lawful wedlock, or wife or widow of the son of the decedent, or the children of the former husband or wife."¹

XII. TAX ON WRITS, WILLS, DEEDS, ETC.

Under the Act of April 6, 1830, certain payments are required by public officers on the issue of writs, entry of judgments, transcript of judgments of justices of the peace or aldermen, recording of instruments of writing, probate of a will and letters testamentary thereof and on a delivery of the commissions of certain officers.

The receipts from these various taxes during the fiscal year, ending the thirtieth day of November, 1905:

Capital Stock Tax	\$8,975,187.89
Corporate Loans	1,922,488.14
Municipal and County Loans	429,621.08
Building and Loan Associations	16,165.42
Stock of Banks and Savings Institutions	900,388.82
Gross Receipts of Bankers and Brokers	61,801.33
Net Earnings or Income	53,680.88
Gross Receipts of Transportation, Transmis- sion and Electric Light Companies	1,536,586.67
Gross Premiums of Domestic Insurance Com- panies ²	110,903.44
Gross Premiums of Foreign Insurance Com- panies ³	1,256,579.59
Personal Property ⁴	3,940,174.95
Collateral Inheritances	1,507,769.03
Writs, Wills, Deeds, etc.	206,926.86
Total	\$20,918,274.10

¹ Act of May 6, 1887, P. L. 79; Act of April 22, 1905, P. L. 258.

² I have added the taxes received from the trust companies as a result of this form of tax.

³ These figures include moneys returned to the local governments.

The other parts of the revenue of the State were derived from these sources:

Bonus on Charters	\$636,323.16
Interest on Deposits	188,078.06
Notaries Public Commissions	12,300.00
Receipts from Licenses	3,021,593.62
Bank Examinations	44,008.71
Miscellaneous	998,346.38
Total	<u>\$4,900,649.93</u>

TAXATION, THE UNIT RULE OF ASSESSMENT; A HOPE FOR THE FUTURE

BY WILLIAM O. MATHEWS

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IN addressing myself to the subject of tax reform, it shall be my object to point out plainly some hopeful results which are apparent in the experience and discussion of the last fifty years, and to show that actual progress has been made toward a solution of perhaps the most difficult of all problems of government.

The power to tax is limited only by the powers of government itself, and in no other field is there wider opportunity for interfering with those fundamental principles which underlie our democratic form of government and which make always for equality and justice between men. With all of equal standing and entitled to equal protection to liberty, life and property, this guaranty can be maintained only at an enormous cost, and each must be ready, be he high or low, rich or poor, to contribute a part or even all that he has — must make an equal sacrifice — in support of the public welfare. It must be understood that revenues are theoretically addressed to persons and not to things; and that, in the apportionment of the burdens, equality must be our first precept; that equality which is human and which prevails in all affairs in life; that, where something is necessary for a common good, the recipients should do their share; should be willing to make an equal sacrifice and suffer the same inconvenience.

We may then say that equality of sacrifice is the measure by which taxes should be apportioned, and in the correct or incorrect application of this principle we have equality or inequality. A careful study of tax administration emphasizes the hopeful fact that our only errors have been in using incorrect methods to reach this ideal. The standard remains high and the solution must come as soon as we understand the vast changes which have

so rapidly revolutionized the sources from which money for taxes must be derived in our country.

History shows us conclusively that the whole civilized world has attempted to enforce just contributions by levying taxes at the same rate directly upon all property of whatever description. It was believed that a man should give up an equal part of all his property, and writers agree that in the early times it was a just tax, but all agree with equal unanimity that time has wrought great changes in the financial and industrial conditions of the world, and that this general property tax no longer reaches to even an approximate degree the ability of our people to contribute to the public revenues, and that it is to the retention of this original system and refusal to reform our laws to meet the new conditions that all our troubles of the present day are due.

What are these changes of conditions and what have we not done to keep pace with them? Is the mass of legislation, by which the world is drifting away from this general property tax, meaningless? Does not the fact that England and France and other leading nations have abandoned the old methods, while we, practically alone, have refused to listen and have redoubled with no results our efforts in almost every State to cling to antiquity, teach us anything? In our private affairs we have learned that our finances must first be correctly adjusted, but in public life a general apathy has brought absolute disgrace, and no one will be found to deny the reign of injustice and perjury and tax evasion. And yet there are hopeful signs, and it is my purpose to discuss the causes of tax evasion and to show that the greatest hopes for the future lie in the application of the so-called Unit Rule in the assessment of the wealth of the State, and that our only progress in legislation has been along its lines.

THE UNIT RULE

As already pointed out, equality of sacrifice involves a payment by each of as much of his wealth as he is able to contribute without putting him to any more or less inconvenience than others. This ability to pay, which has been discussed so much in the books, necessarily involves a proportion of everything possessed by a man which is valuable in money or money's worth. We must understand that it is perfectly possible that

a man may own no physical property whatever and yet be able to pay taxes, for the reason that he may enjoy very large revenues which he spends as he goes, and on the other hand, a man may enjoy no revenue whatever and yet be rich in property and amply able to pay taxes. So that neither physical property nor cash-earning power is an adequate measure, and no proper or equitable system can possibly be established unless everything which makes up the total wealth of a State is reached.

Having settled upon a proper basis of tax apportionment, we come now to another precept which is quite as important as equity, — for without it there can be no equity, — the tax must be levied in such a way that its collection is certain. Here is the battle ground, for the burden of our complaint is tax evasion. In what manner have we failed to reach the volume of wealth of a State? History shows us that in primitive times wealth was made up almost entirely of real estate, and the tax system was satisfactory. Why is the same system not satisfactory at the present time? Writers tell us that it is because in the primitive time the only wealth other than real estate was in farm implements and such other tangible personal property as could be easily ascertained and taxed, and that under the modern system personal property is largely composed of a far more elusive variety of intangible sorts, such as stocks and bonds and credits, which cannot be located by the assessor, and hence escape. It is apparent that this is but a statement of facts, and is in no way an explanation of the difficulties. The problem lies underneath, and an analysis of the tax question shows that the world erred when it adopted the general property assessment. The fundamental principle that a tax in theory is levied on persons was departed from by the assumption that every variety of thing which by physical laws or by legal fiction could be designated as property represented the wealth of an individual. The proposition is not true, and it is a fallacy to designate a share of stock or a bond as property. The wealth of men is not composed of paper or parchment, but is composed of money or money's worth, and we find this wealth at different sources. Real estate is one important source, and another even more important source is trade and business and professions; and a large volume of wealth is not invested at all in these lines, but is held as money

on hand or on deposit in some bank or temporarily loaned. Regardless of economic theories or regardless of our former ideas, these are the facts, and the tax problem must be treated as a distinctly practical question; it cannot be treated as a purely economic question, for many correct economic theories become mere fallacies in practice. It is correct to say that the wealth of every individual can be successfully reached only by searching out these sources, which in the modern practical world are called investments. Now the amount of wealth in the world is immense in its proportions, and it has become the desire of its owners to invest it in order that some advantage may be derived. Usually, the advantage sought is money profits, but it is often true that the advantages are something which the owner regards as desirable as money, or the advantage may simply be some personal satisfaction. With the growth of wealth there has arisen a keen competition to control these investments, and the result is that the real estate or the trade or the business has a value in the community; a value which is the result of many things, including its ability to realize results which are in demand. A successful enterprise may be built up by an individual; or a number of people put together a certain amount of money and contribute their joint experience and wisdom in handling business affairs, and the result is a harmonious, skillfully built and conducted proposition, which you or I or any one else would be willing to pay for as a whole unit if the owners would sell and if we had the money to invest. It is the power of the organization as a going investment, as a production unit, which is of value to us, and it is upon that basis we are willing to pay. To reach each individual owner by taxing the whole productive unit is what is called the Unit Rule of Assessment, and it will be found that when we depart from this practice we make grave errors, and that the only progress which has been made in the legislation of the world has been when its principles have been recognized.

The Unit Rule applies to every form of investment, and it is true that the universal success of the real property tax has been due to its principles. Indeed, real estate taxation stands out as a guide post for us to follow. In all the discussion of tax iniquities it is a fact to be emphasized that the taxation of real

estate at its market value may well remain; and we will do well to note that this success has been brought about by applying a system of assessment which gets at the value of the real estate, not for the purpose of growing crops, not for its cost or what the owner may regard it as worth, not at a price which that same land or building would be worth if it were located alongside of similar property in another city or county, but the universal rule is to tax it for what it is worth for purposes of sale as a productive unit. Some of our largest investments are made in city real estate by groups of men who join their money and property in a unity of use, and there is created a valuable productive unit which is worth far more than the intrinsic value of the clay or gravel and stone used in producing the unit. It is worth the price that people are willing to pay for it. It is that fundamental rule expressed by the supreme court of Ohio, that property is worth for taxation whatever it is worth for sale. This is the only true measure of the wealth of a community, and being the only true measure, we shall never make progress by avoiding it. In the collection of revenues every advantage must be conceded to the government, and there is no complaint in our taxation of real estate that we apparently abandon the theory that a tax should be on persons and seemingly put the tax on the property direct. This is a practical economy which avoids the expense and uncertainty of ascertaining the true owners of the unit and requiring them to pay. It is simpler and more certain to actually lay the tax at the source and let the equities be worked out by the individual owners if they are not taken care of by the rules as to the incidence of taxation. We shall find it necessary to apply this method in many cases in unit assessment, and must remember that its use is justified by the success of the real estate tax.

There is another element which assists greatly in the realty tax, and that is the fact that we do not in any way depend upon the owner either to return the property for taxation or to place a value upon it, but a system has been established by which all the uncertainties of self-assessment have been, or can be done away with. It is very true that unscientific valuations and a system which tempts, in some States, the county officials to undervalue real estate to secure advantages in contributions to

state revenues, have created certain inequalities, but the remedy is in scientific valuation and in removing the advantages to the counties and does not affect the general proposition that the real property tax is successful. It may be claimed that real estate taxation has been successful because it is permanent in its nature, but it is true that all sources of wealth are permanent in their nature, and this constitutes one of the strongest points of the unit system. A complicated system might have been adopted by attempting to segregate the elements of the unit and to ascertain the value of the gravel and the clay and the stone, and then attempting to find the individual owners and levy the tax; and it is quite certain that the system would have been unpopular as, in the first place, it would not have reached all of the wealth in real estate, and in the second place we could not have located the owners and the system would have failed. But we did not do this. We adopted the Unit Rule because, if you go to the source of things, you are apt to find that these sources are more or less permanent in their character.

Real estate is but one form of investment, and there will be no disposition to claim that any different rule should be applied to its assessment than is applied to other forms of wealth. And yet why the undisputed fact that our present methods have failed to reach wealth other than realty? All of the value of real property has been taxed, but it is the experience everywhere that but a small fraction of others' wealth is reached. It is because, while applying the Unit Rule in the valuation of real estate, we have applied to other forms of wealth weak and impossible efforts to divide up the units which are the wealth, and attempt to locate and tax items of physical property owned by the unit. The result has been disastrous, as the method has assumed that people will voluntarily pay taxes, and the assumption is absolutely incorrect. Furthermore, a large part of that wealth is of an intangible sort, made up of a surplus value over and above the value of the physical assets, which investors recognize and are willing to pay for on account of a complete earning unit, and generally speaking, we have made no effort to reach those surplus values. As a whole, the system has resulted in a flagrant discrimination against real estate, and it is absolutely dishonest to continue using the Unit Rule of Assessment unless the same rule

is applied everywhere. To have legislation on the books, which applies a different rule to one class than another, is to legalize inequality, and common decency demands that a change be made.

Far greater in value than real estate are investments of wealth in business enterprises. For the same reasons that people put their brains and money into real estate, they invest also in business, and we have a system ranging from the humblest peddler to the largest corporations with hundreds of millions of capital. It is safe to say that there are fewer business concerns than there are parcels of real estate, and the fact that we have been able to perfect a system of complete records of real estate should encourage us to believe that the government could keep track of and supervise, to the limited extent necessary, every business venture, and by scientific methods, administered by men who hold their office on account of fitness, could with comparative accuracy decide what the particular business is worth for purposes of sale. It is not always necessary that actual sales or quotations be at hand, and a skilled body of men would soon arrive at methods which would be satisfactory to all concerned. The idea of trying to place a selling value upon some business which is not for sale and which is owned by an individual may appear difficult, but we have overcome the same problem in valuing real estate. There are many sections in which the market value of land is unknown or is very uncertain, and yet, by various methods of getting at the opinions of people and comparing these with actual sales in some similar locality, a fair idea is reached, not always perfect, it is true, but so near that a system based upon such valuations, honestly made, would be approximately correct. Sales of business houses are made quite frequently enough to be a basis of judgment. The merchant knows for what price he will part with this productive unit he has created. It is valuable to him far beyond the cost of his stock in trade. The doctor knows the price for which he will turn over his practice. The insurance agent knows the value of his renewal interests; the newspaper is worth a sum which has little relation to the property on hand; while the big corporation has its stock and bonds, which pass from hand to hand and indicate values. You may say that this sounds like a tax upon

thrift and energy. There is no doubt that it is such a tax, but is it not true that all wealth is the result of thrift and energy? Eliminate that element of value and but little would remain. And, again, the thrifty and successful man does not object to paying taxes if he but knows that all are doing likewise. It may also be said with correctness that the professions and small trades and itinerant venders are many in number, and that no accurate system could be devised to apply the Unit Rule, and it is probably true that in many cases some arbitrary annual lump tax would have to be applied, similar to a license tax, the amount to be varied according to the best outward indications to be found as to the class the particular one belonged in; plenty of precedent exists for such methods, and if we are careful to levy the tax so as not to operate as a handicap to discourage people with little or no capital from embarking in the particular line, we shall find it very easy to collect and very satisfactory in its operation, and large revenues will result. There is this objection, that the actual market value of small individual enterprises will not be reached with nice precision, and for that reason we have discussed them first; but whole nations, as France and Prussia, have carried the principle throughout the whole area of business and have used certain outward indications by which they arrived at an estimate of the actual value of the particular business, and a suggestion to apply the methods to these forms which cannot be reached at even an approach to justice in any other way should not be condemned unless better methods can be found.

The first objection to be raised to a business tax will probably be that the business world will not submit their private affairs to public inspection. This objection is a very practical one, and it is true that there are times when a wholesale disclosure of financial conditions might be disastrous to a community, and that at all times the indebtedness of a business is regarded as a strictly private affair. Without admitting that the government would not be justified in securing this information, if necessary, we need not let it trouble us, for the reason that the only real objection would be as to disclosing the degree of solvency of the particular concern, and, as we shall see later, it is not necessary that the indebtedness be revealed. Another

objection might be raised, that a general business tax would tend to discourage new enterprises, but no such result would follow, for the reason that the system we are discussing would bring in enormous revenues, and the rate consequently would be very low in comparison with present rates, and foreign capital would be attracted rather than repelled. This rate, if desired, could be limited by law, and thus any tendency to extravagance as the result of a low rate would also be done away with.

The greatest objection to a general unit rule business tax should be brought out at this point and discussed with full candor. Away down in the heart of each American citizen is a sense of justice between man and man, which is often latent, but ready to kindle at the thought of universal imposition on any particular class. Let the injustices of the present taxing methods but be understood by the mass of the people, and leaders will be found to conduct the nation to a comprehension of the fact that the expenses of government are, in fact, being paid to-day; and that the money is coming from some one; and that it cannot be disputed that the burden of this payment is not equitably distributed; and that the proper share of many is being paid by others, who are perhaps less able to bear it; and that, if we are sincere in our desires to correct these evils, that burden must be removed and placed upon the proper shoulders. We must, and we shall, realize that the taxes of some classes must be increased, and that problem will be met without a murmur if it results in a sound system of finance which bears upon all equally. No State or nation can be great without the elements of greatness, the chief of which is a code of just laws. If a particular class of the public find that a change would increase their taxes, they will be satisfied with the conviction of a duty well performed, and a study of the laws of the incidence of taxation will convince that a tax is often after all paid ultimately by others. Taxes go into expense account and enter into costs, and in the end are paid by the consumer.

The idea of a business tax may be thought to be radical or experimental, but there is abundant proof, the result of experience, to demonstrate its complete success in practice as well as in theory. In developing this argument a review of the history and progress of taxation will completely remove any prejudice

against what may be a new idea to us. The original American colonies were largely agricultural, and the general property tax was seized upon as a just method of levy, and probably did very well under the primitive conditions. But as the colonies developed into a nation, the warnings of history were not heeded. It has been discovered by every nation that economic conditions change with financial development, and that as wealth comes to be made up of property other than real estate, that new wealth is something different than the mere sum of all things which in fact or by legal fictions may be classed as property. Ancient methods will not serve a modern nation, and their retention can be due only to ignorance or neglect. A new and mighty transformation came over our material matters. Where had rolled the lonely stage coach appeared the complicated steam railroad. The value of the coach represented fairly well the wealth in that one unit, but the railroad required financial backing from people all over the country and supplied a demand for the investment of surplus funds which would otherwise be idle. The railroad offered opportunities for increasing this surplus wealth, and the public was willing to pay for this railroad because it was a productive unit. A market value was established by the same conditions which created a market value for real estate. The highest courts of the land tell us that a system cannot be equitable unless we tax a corporation at its market value as a unit, at the price people are willing to pay for it in the same way that we have always taxed real estate. Instead of adapting our system to the new conditions, we simply required the assessor to locate, if possible, the individual items of property, if the corporation happened to own any, and to place an uncertain value upon such property, not for what it was worth to the corporation as part of a going concern, but at a price separated and, in most cases, at the price of scrap, as it had no particular value except as part of that going concern. We flagrantly departed from any chance of equity for the reason that business enterprises had a value far beyond the scrap price of its property. It is a fundamental rule that sale value and tax value should be the same.

This has led us to the discussion of the development of the so-called excess value, or surplus value, or good will. It includes

everything which is of value over and above the value of physical property. There is no reason why railroads should be singled out in a discussion, as the same elements which exist in a railroad or in real estate exist in all other sources of wealth. Other public service companies appeared, and the small trades of our forefathers' day were but the beginning of a wonderful industrial propaganda furnishing a field for the investment of fabulous sums of money. Where brains and money are united, the investor takes into consideration the results of this unity as a safe and profitable venture and bids accordingly for an opportunity to share the profits. Every man who buys into a small shop or a billion-dollar combination absolutely knows that he pays for something more than the mere value of the physical property owned. One company may have excellent prospects of future development of coal or ore or oil or gold, and the public knows it and is willing to pay for an opportunity to be in on it. A parcel of realty is in the direct path of the growth of a large city, and that fortunate fact adds to the value. A manufacturer has excellent patents and a successful career behind him, and this is valuable; a merchant or professional man has a business which he knows is worth a large sum for its good will.

It is of great comfort that we advance when our errors become so glaring that public opinion is thoroughly aroused, and the legislation of the last fifty years shows beyond question that we are slowly moving toward the goal. The seed of dissatisfaction arose early, and has increased with every effort to enforce unjust laws. We are in the midst of a land of abundant wealth, where all classes are prosperous and willing to pay their full share and do not relish the cry of the widow and the orphan and the small home owner. Legislators have been busy, and the doctrine has been developed so far that we need not discuss it in whispers, for in Massachusetts, Connecticut and Pennsylvania they have been for years collecting this kind of a tax from practically every corporation, and the evidence of its popularity and the ease with which it is administered is at hand. Massachusetts retains the general property tax, but levies a special tax at the same average rate on the surplus value of corporations ascertained by reference to market value of stocks and all other information available. In 1905 the tax

on this surplus value alone, not including the property tax, added \$10,500,000 to the revenues. The fact that this tax has been in operation for forty years without any clamor for its repeal is sufficient to satisfy any one who looks upon the proposal as radical. In the midst of the condemnation everywhere heaped upon the general property tax it is most encouraging to read the opinions of investigators of this unit rule tax. In 1897 the tax commission of Massachusetts submitted a report dealing with the whole subject of taxation in that State. Writers agree that the literature of taxation contains no more profound analysis of the whole field of public finance than this document. Hear their report as to the practical workings of the surplus value tax: "Here, then, is no demand for a statement from the individual taxpayers, no doomage by local assessors, no guesswork, no possibility of evading or diminishing taxes by change of domicile, no question of double taxation. The real estate and machinery are assessed locally doubtless not with perfect equality and justice, but probably as carefully as would be possible under any system. The corporate excess is taxed at a uniform rate by the State. The taxes are regular and certain. They are heavy and they yield a large revenue. The rate of taxation on corporate excess for the last fifteen years has been from year to year about $1\frac{1}{2}$ per cent on the capital. Yet little complaint is heard regarding these taxes,—a signal proof that the taxpayers accommodate themselves, if not with ease, at least without serious complaint, to burdens which are steady, regular, predictable, and for which in consequence they are able to make calculations and adjust their affairs. The corporation tax is particularly simple, and is assessed with unerring exactness in the case of large and well-known corporations, whose shares are regularly dealt in and can consequently have a publicly recorded value. Railways, banks, the large manufacturing corporations and others whose stocks are frequently quoted are taxed without a word of inquiry and without a possibility of escape. A very large number of miscellaneous corporations are in a somewhat different position. Their shares are held by a few individuals and rarely transferred, and are without a quotable market value. In these cases the statement required by law from the corporation itself as to the

market value of its shares is important. The tax commissioner may further require a transcript of the balance sheet, and other information which he deems desirable. No doubt there is a possibility of understatement by a corporation of the value of the stock, and a possibility of manipulation of a balance sheet. There is reason to believe that sometimes the taxes on corporate excess are partially evaded in this way; but the evasions are insignificant in comparison with those as to taxable securities."

Connecticut has abandoned the general property tax as to banks, trust companies and insurance companies, and levies a tax of 1 per cent by the Unit Rule on the market value of their shares, and the annual report for 1905 of the state tax commissioners states that the methods have been most successful.

Pennsylvania has abandoned the general property tax, and one of the substitutes is a tax on the entire value, including good will and all surplus value, of corporations and limited partnerships. The corporation is also required to pay a tax for its bondholders, and in this way all domestic bonds are reached without the uncertainty of trying to locate them in the hands of owners. Mr. Roswell C. McRea in states that this unit rule tax is "the banner tax of Pennsylvania's system, and its measurably automatic adjustment to the growth of corporate wealth guarantees a steady increase of revenue from taxation that is not to be expected of tax practice which leaves the listing of property to the initiation of taxpayers or to the guesswork of assessors."

There are but few States which are not using the Unit Rule in one form or another. Illinois, Indiana, Minnesota, Mississippi, Nebraska, North Carolina, North Dakota, South Dakota and Tennessee specifically defined corporate excess as taxable property in one way or another, while in five other States shares are taxed at full value to the shareholders and the corporate excess thus reached. The laws of Hawaii contain perhaps the most advanced legislation in a provision that "where property of several kinds is combined and made the basis of an enterprise for profit, such property shall be assessed as a whole at its fair and reasonable aggregate value, and in making such assessment net profit, gross receipts, actual running expenses, the market price of its stock and all other facts which

reasonably and fairly bear upon such valuation are to be taken into consideration." There is also an income tax upon the profits of property, business, trades and professions to reach surplus value.

Next in importance to real estate in investments is the railroad, and the Unit Rule has been freely used in response to the demands for better methods to require all wealth to pay a fair share of the taxes. Its application to railroads has proven that the Unit Rule is unerring in its efficiency, and the taxation of the whole field of public service corporations has been completely revolutionized. It is safe to say that under the general property assessment the railroads could be reached for but 10 to 25 per cent of their true value, and in no other way than by the Unit Rule of Assessment can the whole value of that fruitful source of wealth be reached. A study of the legislation as to railroad taxation shows that almost every method under the sun has been applied to tax them more adequately, and the righteous war being everywhere waged by railroad capital against what is, in fact, an unjust discrimination against them will continue until the Unit Rule is applied everywhere and to all classes of investments alike; but the railroads will scarcely be able to stem the tide which has set in against them, for the reason that the portion of the population which holds the balance of power in legislatures is alive to the fact that the old methods are inadequate, and their representatives will listen to the demand that as large a mass of wealth be taxed by additional methods, and will feel justified in the belief that, even if it be an unjust discrimination, there can no harm result, as it but transfers an unjust burden from one class to another better able to bear it. The situation should be dealt with at once along broad lines, as it is dangerous to our form of government to allow legislatures to legalize inequality. That there is no difference between the surplus value of a railroad and that of an industrial corporation is quite apparent, and yet but two or three States apply the Unit Rule to all corporations. That there is no distinction between this surplus value of a partnership or an individually owned enterprise is as certain, and yet no State applies the doctrine to a strict logical conclusion, although Pennsylvania with a supplementary system of mer-

cantile taxes has gone far. That mystic thing which prompts men to be willing to exchange money or money's worth for an interest in a productive unit is the same everywhere; it is called "value" and is made up of many ingredients. The legal right exists to tax the railroads for all of this value. The same rule applies to every line of business; its success is more or less dependent upon a favored situation, which the people have themselves created, and the demands of the largely increasing number of people for the particular commodity furnished, and the business, as a whole, is made immensely valuable—largely an unearned increment.

In the beginning of railroad history the general property tax was universally depended upon, but in forty States additional levies are now made to reach surplus value. Delaware, Maine, Massachusetts, Minnesota, Pennsylvania and Wisconsin seem to have practically abolished the general property assessment of railroads; Connecticut, Minnesota and Wisconsin levy no direct tax whatever on property in use for railroad purposes, and reach the whole value of the unit in our operation. Connecticut taxes at 1 per cent the true value, and requires the board to consider quoted prices of stocks and other knowledge at hand, and requires that the floating debt or bonds be not deducted, but be taxed at the same rate as their par value. Minnesota reaches the total value as a unit by a tax on the gross receipts, while Wisconsin, after careful consideration, has adopted the *ad valorem* system of unit rule valuation in the place of a former tax on gross earnings. Maine taxes the real estate and levies on the gross receipts; Delaware levies 1 per cent upon the actual cash value of the unit and retains other methods; Massachusetts on the same basis, with real estate and machinery taxed direct and deducted; Pennsylvania levies the unit rule tax at one half of 1 per cent and has also a gross receipts tax and a tax upon certain real estate. Twenty other States levy a unit rule tax on gross earnings, which is supplementary to the general property tax, seven on gross receipts, one on net income, one at a stated sum per mile and seven have a special franchise tax on shares. Ohio retains the general property tax and has a supplementary tax on gross earnings and a special franchise tax of one tenth of 1 per cent. Since 1901, Michigan

has used an *ad valorem* method replacing a gross earnings tax. New York has a unit rule tax based upon dividends or gross receipts. Kentucky also levies on the value of the capital stock.

It is impossible at this time to differentiate properly these various methods, and it is sufficient for us to note that the universal objective point has been to apply better methods to reach wealth which the general property tax has left untouched. While the movement has subjected trunk lines to attack by different methods in different States and has created some double taxation, yet the Unit Rule is logical, and the inequalities are almost entirely the result of interstate complications and the failure to understand the universal nature of excess value over and above physical property, and these are matters which will be remedied with a correct understanding of the situation.

It is instructive to note that in 1891 the Pennsylvania Tax Conference, made up of representatives from the different classes of taxpayers of the State, made an elaborate study of railroad taxation, and reported in favor of the Unit Rule and stated that the debt capital should be included.

Bulletin Number 21 of the Department of Commerce and Labor places the total value of railroads in Ohio, reached by capitalizing earnings, as \$690,000,000. When we find that under the general property tax the valuation was \$134,000,000, but 19 per cent of the true value, some idea of the reasons for specific railroad taxes are made clear. This same bulletin places the value of railroads in Connecticut at \$105,000,000, and we find that under the Unit Rule the valuation was \$120,000,000, the excess being probably accounted for by the fact that the Department of Commerce capitalized the earnings while Connecticut was guided by the market value of stocks and bonds. Here is a convincing demonstration of as thorough taxation as was ever applied to real estate. What could be more ideal if we but apply the same methods to all productive units.

There has been a great deal of discussion as to the merits of the gross receipts or gross earnings tax to reach this ideal. No reliable valuation can ever be made without considering earnings and gross receipts, because actual sales are often made under extreme conditions which do not reflect true value. But the same difficulty is always present in valuing real estate.

The difficulty of getting at fair valuations, if made by men who understand the situation, have been greatly exaggerated. If stock quotations are abnormally high or low, that fact is known by experts, and constant familiarity with values will work for accuracy. Earnings should always be considered along with sale prices, and in most cases the valuation would of necessity be computed almost entirely from earnings, as even in railroads the proportion of quoted stocks or bonds is very small. The California Tax Commission of 1906 reported in favor of the Connecticut method of considering quoted prices of stocks and bonds in connection with all other information obtainable, saying that it is easy to administer and imposes no unbearable load on the companies, and is, as nearly as may be, an accurate and scientific method of taxing the property of a railroad at its real market value. The fact that both Michigan and Wisconsin have, after most careful experience and study, changed from a tax on gross earnings to the sale value is also significant. Experience has shown that the keeping of accurate accounts can be enforced, and many years of successful practice insures satisfactory results. There can be no sufficient reasons for relying entirely upon earnings as the best measure of market or sale value as there are many enterprises which have no real earnings for years. Sometimes a competitive policy forbids profits for a long term of years, but a good will is being built up, and this is valuable. A company may be very valuable, and yet never make a dollar of profit, for the same reason that real estate may not earn anything and yet be in the path of increased value for the future. A proper system must surely follow the methods which have been successful with real estate, and the fixing of unit value should be a concrete production, the result of all experience, expert knowledge and common sense. Quoted prices cannot be relied upon solely, as the stock exchanges often make fictitious values. A stock may be run up or down by speculation or sudden unfavorable news or by the supply of money available for speculative methods. Nor can earnings be the sole guide, nor gross receipts, for the margin of profit differs in every line of business and on every railroad, and the gross receipts method is unequal.

The problem of arriving at this unit rule valuation, where every dollar of taxable value is found and taxed once and for all, has been dealt with until it no longer presents an unsurmountable aspect. The Department of Commerce and Labor has valued by the Unit Rule every railroad in the United States, and there has been evolved a working system, satisfactory in its results. Professor Henry C. Adams, assisted by Professor M. E. Cooley, of the Engineering Department of the University of Michigan, made for the State of Michigan a technical inventory of the physical value of the railroads of Michigan, in order that they need not depend upon reports of the companies. Every mile of line was scientifically inspected by experts and valued, and the intangible surplus value was ascertained by capitalizing earnings and comparing them with quoted values of stocks and bonds when available. We cannot go into the details of valuation methods, but there is one fact which stands out clearly: all valuations of railroads or any other wealth must be made by experts and by men who are entirely free from political influence. The financial man in private business is one who is skilled by long service and who knows that rewards will come with increased efficiency. No success can ever be expected so long as tax officials are chosen without any regard to their fitness for the work. While our tax systems have been wrong, they have been administered largely by assessors and officials whose very positions depend upon the friendship and votes of those whose property they must value. The tax system of England, as far as administration is concerned, is a marvel of thoroughness, and it could not be so except for the fact that the positions are practically for life and the officials are experts. The Uniform Public Accounting System, so successfully operating in Ohio, has also great possibilities in securing the best results from a unit rule system.

The legality of the Unit Rule of Assessment is unquestioned. Not only state courts but the Supreme Court of the United States has fully decided that the only method by which all the wealth in a going concern can be reached is by the Unit Rule. Mr. Justice Miller, in the State Railroad Tax Cases (92 U. S. 775), in deciding the right to consider quoted prices of stocks and bonds, said: "It is therefore obvious that when you have

ascertained the current cash value of the whole funded debt and the current cash value of the entire number of shares, you have, by the action of those who above all others can best estimate it, ascertained the true value of the road, all its property, its capital stock and its franchises; for those are all represented by the value of its funded debt and of the shares of its capital stock." Mr. Justice Brewer of the United States Supreme Court in upholding the express company cases referred to the fact that the actual value of the corporation was \$16,000,000 — a value which could be realized by its stockholders at any time — and that the tangible property was worth but \$5,000,000. He pointed out the injustice of requiring the protection of property having so high an actual value and limiting the tax to the value of the tangible property, and said that "courts must recognize things as they are and as possessing a value which is accorded to them in the markets of the world."

The other classes of public service corporations have felt the advance of the unit rule movement, and the last twenty years of legislation shows that sleeping car, parlor car and fast freight lines are subjected to that method in twenty-six States. Eight States apply the sale value rule to that proportion of the total value represented in the State; twelve States reach the surplus value by taxing gross receipts; two tax gross earnings; three apply a fixed annual tax; while one taxes net income. Most of these States still use the general property assessment and the unit rule taxes are additional; and in some of the States, as in Ohio, still other specific taxes are applied, no one of the methods carrying out the Unit Rule to its logical conclusion, to tax the company but once and then for all it is worth.

Express companies are now almost universally reached by the Unit Rule. Seven States tax the sale value of the business in the State, while over twenty apply the gross receipts method and six use a license or fixed annual charge.

Telegraph and telephone companies are subjected to the sale value method as a whole in six States, gross receipts tax in seventeen, and a fixed sum per year or per mile of wire in eight States.

Insurance companies are subjected perhaps oftener to other class of investment to these specific unit rule

make up for the deficiencies of the general property assessments, and we find a tax on gross premiums in forty States, while the remaining States use net receipts as a basis or apply a fixed license.

In addition to the various methods we have described there is levied in eighteen States an annual so-called franchise at a low rate, which applies to all corporations and which has no other justification except to carry out to a limited degree the principles of the unit rule method. It is sometimes said that this is a proper tax upon the right to continue to be a corporation, but the practical side of the question is that a tax is a tax and the genesis makes little difference to the one who pays.

Suburban and street railways are generally subject to the same specific taxes as are railroads and have the same ground for complaint of discrimination. The Massachusetts Commission of 1897 reported that they had not considered any peculiar or exceptional methods of taxing public service corporations and assumed that they should be taxed on the same principles applied to persons and property in general.

There is a form of license tax which in fourteen States is an important part of the revenue system and intended to take the place of the general property assessment. This does not refer to the minor municipal licenses nor to liquor licenses, but to a method of assessment which has many merits in reaching the full value of a going concern. If some practical method could be evolved to classify business by some outward signs so that a fair degree of equity could be achieved by applying a license graded according to class, the method would be worthy of serious consideration, for it is the simplest of all taxes to collect, and the one who pays would always know what his tax would be. Its use has been confined largely to the Southern States, although Pennsylvania and other States have used it successfully. It is distinctly a unit method of assessment, arrived at without the detail of ascertaining sale value.

Another practical demonstration of the utility of the Unit Rule is found in the various statutes applying to banks. The federal laws forbid any taxation of national banks except upon their shares, and this has led to an almost uniform method of taxing the value of shares of all banks, which tax, however, is

usually paid by the bank. The general property assessment is not used except perhaps in California and Nevada. The result is that the value of the whole bank is ascertained, and then it is apportioned to the shares. The book value, however, is used instead of the market value, but it is much more effective than property tax, and has resulted everywhere in taxing the banks more severely than other business. The federal statutes allow of the shares being valued at their actual cash value, and this would put banks upon the same footings as all other wealth if the Unit Rule were adopted generally. In Connecticut we find the full Unit Rule applied, and banks, investment and trust companies pay 1 per cent upon the sale value of the aggregate of their stock; Virginia levies on the sale value of the shares, as does also Indiana and Massachusetts. This is the true unit principle and would be eminently fair and satisfactory if uniformly used.

ENGLISH INCOME TAX

The British Income Tax is essentially an application of the doctrines of the Unit Rule of Assessment, not carried, however, to its full extent; as, while they seek not all sources of wealth and endeavor to reach the full taxable value, they measure this value by the actual money earnings instead of ascertaining the selling value; while they fail to consider earnings or benefits other than money and thus fail to reach all of the value, yet the attempt is to get at the actual value of each source of wealth as a productive unit. In order to reach the value of real estate as a productive unit, taxes are levied in proportion to the rental value, which tax is assessed to the occupier; the corporations pay taxes according to their profits, and the theory is that the actual value of the interest of each stockholder is thus reached. Those who are in general business pay a tax on the value of that business, ascertained, not by the value of this property owned, as under the general property tax, but by the value of the business to them as a productive unit as measured by its profits, thus reaching all the earnings of good will. Trades and professions are taxed in the same way, according to the profits accruing to the person, and good will necessarily enters into these earnings to a certain extent. The point to be remembered

is that the British Income Tax is a departure from the erroneous rules of assessment embodied in the general property tax, and that in ascertaining the ability of each citizen to pay taxes, it goes to the source of wealth and takes a portion based upon the value of that wealth as a productive unit; the tax is levied upon the earnings of industry, and as earnings are largely the product of good will, it follows that good will is taxed.

The income tax is popular in England and has met with little change in the last fifty years. It is true that inequalities exist wherever self-assessment has been retained, but on the whole there seems little demand for repeal. The tax is collected by the national government, and is free from our interstate complications, and produces large revenue at a small cost of collection, and is free from the great inequalities between the contributions from different classes of property caused in our country by applying a unit rule of assessment to real estate and an inadequate property tax to other forms of wealth.

Another result of the English Income Tax will appeal to every citizen, the fact that the officials agree that evasion amounts to but 15 per cent of the total property taxable, a large part of which is foreign stocks and bonds which have never been reached by any system and which after all are in the doubtful list of double taxation. This very thorough assessment has resulted in a very large duplicate and a very low rate, approximately 5 per cent of the income; this is but one twentieth of the income, and is in strong contrast to the fact that our general property tax seeks to appropriate an amount ranging from one third of the income to entire confiscation, an income tax of from 30 to 100 per cent. And it should be emphasized that this remarkable result is not caused by the strict income tax principles with its self-assessment, as the English system is not, in fact, an income tax, but it is largely a unit rule system of assessment based upon income; personal returns of owners of shares or realty are not depended upon, but the tax is levied at the source of wealth; the real estate or the one who happens to be in possession of it pays the tax, and the tax on shares is levied on the corporation. Assessment at the source of income is the feature of the English system. This is possible where you apply rules which reach once and for all the entire tax

value. These sources of wealth can be made amenable to public regulation; they are not so numerous, and the practice of self can be largely eliminated.

FRANCE

In France every person who carries on a trade, business or profession is subject to a business tax, which aims to reach all profits from industry. The law selects some outward indication by which the value of the business is measured as a productive unit without resorting to personal returns.

PRUSSIA

The Prussian government also levies a unit rule tax upon all business, and, like England and France, seeks the true value of the enterprise as a going concern by taxing the business according to its capital and earnings.

SINGLE TAX

The Unit Rule comes into immediate conflict with the so-called single tax theories, which have been looked upon with a certain respect and are advocated by many public-spirited men; but the large weight of authority is opposed to even the consideration of so radical a change, which would necessarily carry with it a revolution of our ideas as to beneficial ownership of land. Whether the system would bring any worse results than our present laws need not even be discussed, for it deals with social theories beyond the realms of taxation, which should be disposed of before we condemn the right to tax all wealth according to our thoroughly established practice.

TRADES — PROFESSIONS

When we have discussed realty and business in general, there remains professional practices, trade earnings and wealth derived from other sources which cannot be reached except by special means. These, perhaps, do not come within the principles of the Unit Rule, although the good will of professions is often sold and the decisions of courts recognize it as valuable property. Here it will probably be necessary to resort to personal returns or to some graduated scale of taxes, but

we need not dwell upon the problem except to say that in many cases the one who pays over the income or profits can be required to pay the tax as the agent of the government. This is the practice of stoppage at the source which is so successful in England, and it can be applied to all business houses or government offices which pay incomes over and above the proper exemption. If we can find a way to reach such income, then all the wealth there represented will be reached.

FOREIGN STOCKS AND BONDS

In a complete unit rule system there would be no necessity to tax stocks or bonds; as, if all wealth were taxed at its source, it would be wrong to again tax the mere paper which evidences that wealth. We would scarcely think of taxing a partnership for all that it is worth and again taxing the agreement which represents the ownership or interest of each partner, nor do we think of levying upon a deed where the realty represented by the deed is located in another State and taxed there. To assess shares where the property represented by them is located and taxed in another State is simply double taxation, and yet to carry out this principle would cause as great an injustice to each State for the reason that, on account of the independent sovereignty of each commonwealth, there is no jurisdiction to reach the productive unit located in another State, and a condition would be brought about where all the advantages of government would be furnished to many men of great wealth and the particular State would be deprived of any revenue. It is obvious that some provision must be made to overcome this difficulty, and there is ample justification for a tax at a rate which shall be very moderate. It is sought generally by present methods to tax foreign securities at a rate which amounts to confiscation, and it is impossible of enforcement, while the threat of taxation drives capital to other parts. All other nations levy this tax at a low rate, which seldom exceeds four tenths of 1 per cent. A very large investment class is being developed in this country, and state lines are being entirely eliminated, and the necessity may soon be shown for using the federal government as a clearing house for the enforcement of a unit rule system where the owners of enterprises live in

other States, the receipts to be paid to the different States upon some equitable basis. Even a low rate levied direct upon the securities will never be satisfactory, as gross evasion cannot be prevented, and the practice tends toward bad government by breeding disrespect for law.

It is generally conceded that stocks should not be again taxed where the corporation is already reached by the particular State, and the same rule should be applied to domestic bonds. Bonds represent an indebtedness and, in theory, should be deducted from assets when finding the valuation under the Unit Rule, but no one will maintain that the bonds should also escape in the hands of the owner. The difficulties of reaching these bonds in the hands of the owners preclude that method and justifies requiring the company to pay the tax on its indebtedness, leaving the equities to be worked out between the company and the owner of the credits.

NOTES AND MORTGAGES

This same rule should apply to all credits. Economically speaking, there is no new wealth created when a man contracts a debt. By loaning money a man does not increase his wealth, nor does the borrower become poorer thereby; its effect is as the temporary loan of a chattel. It is necessary that all the wealth represented by the transaction be reached, and anything further is double taxation. Where the debtor can be reached and not allowed to deduct his debts, no attempt should be made to tax the creditor. This doctrine is generally admitted in the matter of mortgages, and the principle is the same as to all credits. Where the debtor or the property by which the debt is secured is in another State, the foreign credits should be included in a low tax rate.

DEPOSITS

The deposits of a bank are a debt to its depositors and, theoretically, should be deducted from the assets of the bank in arriving at the value of the bank for taxation, but this assumes that the deposit will be reached in the hands of the depositor. Money in bank is simply surplus wealth which is not reached in any other form, and it must contribute to the

public expenses. It is impossible, however, to collect the tax from a myriad of individuals, and the tax should be paid by the bank, which should be given the right to reimburse itself from the depositor. Some have claimed that deposits should be exempt; but it is scarcely possible that a rich man with money in every bank should escape entirely, while the poor man who transfers his savings to a small home should immediately be seized upon.

TANGIBLE PERSONALTY

In an analysis of the Unit Rule it must be observed that its principles have no application to that portion of wealth made up of tangible personal property except as it is included in the valuation of some productive unit. It will then be reached without escape and without the systematic undervaluation under the property tax. There is a vast amount of difference between the amount for which personal property is carried on the books of a company as part of a going concern and the estimated value as a separate piece of property, and this will greatly increase the tax duplicate.

It will be but common decency to use a method of valuing the personal property not used in business, which shall be as thorough in its operation. State commissions of New York and Massachusetts have favored a habitation tax to cover such property, and for the limited purpose we are discussing such a method should bring good results. The size and cost of a house is a fair indication of the value of the contents, and the value of a stable should also indicate to a fair degree of accuracy the horses and carriages; and a special levy upon occupied real estate, at a proper rate, would be infinitely superior to present methods. By requiring the owner to pay the tax it could be collected with the regular realty levy at great economy, as the whole costly system of valuation by special assessors could be done away with. The owner should have the right to recoup from the occupant, and the plan could be worked out to reach all farm implements, crops and live stock. The farmer would then be upon the same basis as others, while at present he is subjected to gross discrimination. Some idea of the economy of the plan is apparent when we consider that

the entire contents of immense office buildings and apartment houses could be taxed by a few strokes of a pen, and there would be no escape and no cost of collection.

CONCLUSION

By way of illustration as to the financial results of the assessment methods we are discussing it may be noted that in one State, Ohio, in the year 1906 the total taxes collected for all purposes amounted to \$60,000,000, as shown by the report of the auditor of state. If we can ascertain the actual value of all wealth in the State which would be reached by the unit rule, we can, with some degree of accuracy, forecast the rate of taxation necessary to produce this revenue. The report of the Department of Commerce and Labor, on Wealth, Debt and Taxation, gives the following results as to the total value of all property in Ohio in the year 1904:

Real estate and improvements	\$3,383,835,000
Live stock	173,847,000
Farm implements and machinery	38,550,000
Manufacturing machinery, tools and imple- ments	216,948,000
Gold and silver bullion and coin	90,599,000
Railroads and their equipment	689,797,000
Street railways, shipping, waterworks, telegraph, telephone, electric light, Pullman cars, and private cars	329,197,000
Products of agriculture, manufactures, mining, imported merchandise, clothing, personal adornments, furniture, carriages, etc.	1,024,197,000
Total	\$5,946,969,000

As will be seen, this does not include the value of business enterprises as going concerns except in the case of railroads. The item of "manufacturing" shows \$216,000,000, while a report of 1905 of the same department states that the capital invested in manufacturing in Ohio is \$856,000,000. Again, the above estimate makes no mention of intangible stocks and bonds owned in the State, which must run into hundreds

of millions. Banking capital is not included, nor are deposits in banks, which in Cleveland alone amount to \$232,000,000 and must exceed \$500,000,000 in the State.

Our discussion has shown a method to reach all this vast volume of wealth, amounting to over \$8,000,000,000. This figure is undoubtedly conservative; and a rate of taxation applied to all of it of $\frac{3}{4}$ of 1 per cent would raise all the revenue necessary in the whole State of Ohio. It is possible to reach every dollar of \$8,000,000,000 of wealth in Ohio, and there is room for little doubt but that the application of the Unit Rule of Assessment in Ohio would reduce the tax rate throughout the State to 1 per cent. In making a report to the Governor of Connecticut, the tax commissioner of that State, in 1905, said, "I firmly believe that if all property within the State of Connecticut were assessed at a fair valuation, that a 1 per cent rate of taxation would produce as much revenue as is now raised by the rates varying in different towns from 1 to 3 per cent." Other writers have stated that a rate of 1 per cent is high enough. Any system which does not reduce the tax rate on real estate to near this figure will be a failure. What greater hope is offered to the farmer and to the home owner and to realty in general? A tax of but 1 per cent on real estate means lower rents. The removal of double taxation on mortgages means lower interest charges. A tax rate of 1 per cent means increased prosperity to all, and it means a far richer and nobler manhood in increased respect for law and encouragement to believe that the object of law is justice.

Under the present laws in Ohio, banks and trust companies pay more than their share; as do express companies and insurance companies; as do all owners of real estate; as do the widows and the orphans. Two hundred and fifty thousand farmers are taxed unjustly. The owners of foreign stocks and bonds do not pay their share. The business man, in general, does not pay his share. Railroads and other public service corporations have paid at the rate of about $\frac{7}{10}$ of 1 per cent on their unit rule value. It is certain that this rate should be increased to 1 per cent, and it is in every way desirable that the present widespread complaint that railroads are not paying their share of the taxes be ended. In Connecticut and possibly other

States the railroads pay as high as 1 per cent on the selling value of their road as a productive unit. There seems to be no reason to suppose that the railroads will object to paying taxes under the same rules which are applied to all other forms of wealth. If the present disgraceful discrimination is to be cured, it is certain that the burdens of some class must be increased. Business taxes are ultimately paid by the consumer, and profits will scarcely be less, while the shifting of the tax will not bear upon any one with any hardship. The knowledge of a duty well performed will result in the richest of dividends. A multitude of owners of foreign securities will pay a fair tax, and, if necessary, this can be largely enforced by requiring banks or other agencies which distribute dividends or interest or which hold the securities as collateral security to collect the tax as the agent of the State and thus do away largely with the uncertainties of personal returns. If this tax is fair, no one can complain of strict provisions for its enforcement. Without such it will be a farce.. People in professions, numbering 77,000 in Ohio, will augment the revenue, and as many more in other occupations who do not now contribute their share will be asked to assist. An enormous saving will be brought about through the possibility of public accounting in tax departments and by doing away with the expensive machinery of boards of equalization. A system with hopeful possibilities will create a desire for scientific administration, and great economy can be brought about by the establishment of the merit system. Other reforms can be accomplished, such as the extension to other departments of the cash recording fees now in force in recorders' offices. There seems to be no reason why all departments could not be run on a cash basis as is the national post-office department. A special mortgage recording tax now in successful operation in New York would not be double taxation and would largely increase the revenues.

With large revenues and strict economy in administration the Unit Rule of Assessment will make it possible to better perform a duty which every State owes to itself, that of providing sufficient funds for the proper education of the youth of the State in localities where wealth is scarce and children are

plenty. Each State should likewise have sufficient money to carry out a system of good road building; the advent of the horseless vehicle but emphasizes a condition which has greatly handicapped the farmer and the general trade of the whole State.

As has been said, the Unit Rule has the full support of the highest courts. The Supreme Court of the United States (166 U. S. 185) has used this unmistakable language: "Whenever separate articles of tangible property are brought together, not simply by a unity of ownership, but in a unity of use, there is not infrequently developed a property, intangible though it may be, which in value exceeds the aggregate of the separate pieces of tangible property. Upon what theory of substantial right can it be adjudged that the value of this intangible property must be excluded from the tax lists, and the only property placed thereon be the separate pieces of tangible property? . . . Now, it is a cardinal rule that should never be forgotten that whatever property is worth for the purposes of sale it is also worth for the purposes of taxation."

There is one principle which must be observed in the application of the Unit Rule or we shall find ourselves in the position of levying a tax upon interstate commerce and thus violate the very foundations of our federal Constitution by taxing property which has its being and is already taxed in other States. Take the case of the New York Central Railroad with its terminals in New York State costing perhaps \$50,000,000. This line runs through neighboring States, and each has the legal right to levy a tax by the Unit Rule; but the valuable terminals are a part of the unit rule value of the system, and it is manifestly incorrect for another State to include any property, in ascertaining what proportion of the entire unit value of the system should be taxed in the particular State, which has already been taxed in another jurisdiction, at least at no more than a very small rate. Railroad capital and its free investment is of the greatest importance to the prosperity of any community, and any tax system must be fair to them to merit its support.

By doing justice to all, we can require justice and can win for these United States the race being run in every tax district

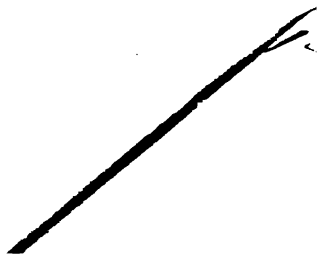
in the world. The methods of the Unit Rule are the creation of the effort of a half century of thought and our only progress has been along its lines. Very conservative States have carried the principle very far in applying it to all corporations. What reason can there possibly be for not extending such successful methods to their logical limits? There exists as much demand for one line of investment as another. We would not regard it as inequitable to tax the shares of domestic corporations at their full selling value if the property of the company were not taxed; and this is what the Unit Rule accomplishes, and nothing more. Our present methods are resulting in practically a single tax upon realty. The Unit Rule of Assessment is a property tax which actually reaches all property; it is all that is good in an income tax, without the bad.

Good authorities recognize the main principles of the Unit Rule and no literature is to be found opposing it. Professor H. C. Adams has been its foremost advocate as applied to railroads, and in his report to the Michigan Tax Commission he calls attention to the existence of surplus value in all corporate enterprises. The California Tax Commission of 1906 reports: "There is no doubt whatever that there is an element in the value of corporate property which is over and above the values of the physical and tangible property. If the corporations were taxed upon any equitable basis which referred to their earnings, the vexed question would disappear." Mr. Judson, in his work on taxation in Missouri, in discussing the development of the Unit Rule to corporations, says that it arises from a sense of justice that all the wealth protected by the State should pay taxes. The United States Industrial Commission, in its report of 1902, recommended "that the general property tax upon real estate and tangible property be supplemented by special taxes or licenses upon any business that is not, by the general property tax, made to bear its just share." The report of the Wisconsin Tax Commission of 1903 states: "The unmistakable importance of corporate taxation at this time renders the adoption of a rational, harmonious and efficient system a prime necessity. The wealth of the country consists largely of investments in corporate securities, stocks and bonds in railroads and other corporations which are not

and cannot be reached for taxation to the holders by the severest and most inquisitorial laws. The taxation of corporations as legal entities is the only recourse, and therefore the method to be employed is of considerable significance. The highest authorities on economic and public finance are of the opinion that the problem of just taxation in this country is largely the problem of corporate taxation." Professor Seligman has said (4 Publications, Mich. Pol. Science Asso.), "Let us try to keep the real estate tax for local purposes and supplement it by a tax on corporations, inheritances, and on carefully selected occupations through a system of license taxes." Mr. F. C. Howe, before the 1901 Conference of the National Civic Federation, said, "There seems to be no good reason why such a method of valuation, based upon stocks and bonds, should not be extended to all classes of corporations, including those organized for mining, manufacturing and general industrial purposes." The Supreme Court of Ohio calls attention to the fact that we tax good will in real estate and holds that it is but equitable to tax the good will of a corporation. A report of a Joint Special Committee of the Legislature of Massachusetts, in January, 1907, calls attention to the fact that "public service corporations now contribute more nearly their fair share to the public revenues than do the public service corporations of other States . . . the system is based upon the principle that the best way in which to measure the property and franchise values of these corporations is by a determination of what the public will pay for them." The California Commission of 1906 holds that it is a question open to serious consideration, whether the taxation of such a franchise, tantamount to the taxation of the good will, against corporations, while similar items of property are not assessed against individuals and firms, does not constitute an unjust discrimination. Professor R. T. Ely has said, "There is no reason why ordinary business corporations should be taxed differently from individuals or partnership business." Professor Adams, in his work on "Public Finance," says, "The chief reliance of the revenue system should be the business taxes."

If wealth is the proper measure of the ability of a man to pay taxes, and if we concede, as we must, that the good will

or surplus value of every business or profession represents a large part of that wealth, then how can it be possible for any one to believe that we can ever have equal taxation, how can property other than real estate ever be required to pay its share, unless we tax good will or surplus value or excess value wherever we find it? Let us accept the situation as it exists, and, by considering this one proposition as settled, we shall have made more progress in practical tax reform than has been brought about in the last fifty years.



GOVERNOR GUILD: I now declare the meeting open for discussion.

MR. CORBIN (Connecticut): One or two of the speakers have honored Connecticut by mentioning her. It appears to me that Connecticut has one or two features which are rather unique. Her constitution has no mention whatever of taxation. All of her rules, customs and procedure in reference to taxation are derived from statute. When Professor McPherson quoted from the commissioner's report, that was a report of nearly twenty years ago, nearly twenty-six years ago, when there was a state tax. The last special commissioner Connecticut had was in the middle of the '80's; since that time the state tax has been entirely abolished, so that we have now what many speakers have lauded, an entire separation of state and local taxation. Our local taxation is confined to the taxation of real estate and personal property, with many exemptions. Our state tax is confined to the taxation of corporations, with the addition of an inheritance tax. In addition, however, the State gets the benefit of a four mill tax per year, which is peculiar, I think, to Connecticut, although Pennsylvania has one very similar, on choses in action, notes, mortgages, etc. The persons who take such things must have them registered and pay a tax of four mills per year, and then those securities are thus exempt entirely for that length of time in the State. Before this system was adopted, the small amount of notes and such securities held in Connecticut was notable, but after this rule was adopted, suddenly there came to be a large amount. It seems to me that four mills just about determines the amount that a person is willing to pay to satisfy his conscience so that he would not have to commit perjury; and certainly from the standpoint of the State of Connecticut it is a very satisfactory method of taxing such intangible property.

As has been mentioned here by the last speaker, the railroad tax is a tax of 1 per cent on the market value of stocks and

bonds. The stocks of all investment companies are taxed in that manner, and are exempt, all of these, in the hands of holders. In addition we exempt moneys loaned on mortgages, provided the borrower will agree to pay the tax on that money; but moneys loaned on mortgages outside the State are taxable, but those securities may be taken to the treasurer's office and the tax of four mills paid. The tax on investment companies and on corporations, 1 per cent tax, includes, however, a local tax which is paid to the town in which these companies hold real estate; but that tax is deducted from the 1 per cent tax before the taxation is made by the town upon that investment company. So that it seems to me, after hearing the theories presented here, that Connecticut has many advantages.

You will all recall that in 1787 Connecticut made a suggestion which is called now the "Connecticut Compromise," which resulted in the adoption of the Constitution of the United States. It may be that some of these little features which the small State of Connecticut has, if adopted by other States, may effect a compromise which will do away with a lot of trouble about taxation throughout the United States.

MR. FROST (Washington): We have in the State of Washington the largest forest area within the confines of the United States, great timber tracts. We have there trees so large that when fallen upon the ground it is necessary to go around the tree because you cannot climb over, and there are several trees so large that you have to look several times before you can see the top. We are compelled under the general property tax to contribute to the support of local institutions throughout the State. I might say in passing that we are not hampered in the State of Washington by any popular prejudice. The State of Washington is populated by people from all ends of the earth, and each one brings his own peculiar prejudice with him, and the result is we have never been able to recognize them, and where we have no precedent of our own we simply are compelled to establish one.

We are compelled to contribute especially to the schools under a school board law. The schools of the State of Washington are supported by state taxation, that is, by taxation of all the property in the State. The law requires the State Board of

Equalization to levy a tax upon all the property in the State, sufficient to secure for each person of school age the sum of \$10 in the State of Washington. The teachers' wages and all the ordinary expenses of maintaining the schools are borne out of this state fund. The fund is distributed to each school within the State upon the average number of pupils of school age. The result of that is to lessen local taxation and to compel the corporations and the large timber rentals of areas to contribute very heavily, very liberally, and the further result is that we have one of the best schools systems in the United States and pay the highest wages. In addition to that, we levy annually one half of one mill upon all the property in the State for state highway purposes. We have a provision in our law, if in any locality they desire any highway, they may get a commission, first making application to the board of county commissioners, then to the state commissioner, and the local community bears one half the taxes, and the other half is borne by the State. The result is that the farmers throughout the State are now starting a system of macadamized roads. In addition to that the principal thoroughfares are called state highways and are being built entirely by the State, and we are employing the convicts of our penitentiary in the construction of these roads, supporting them from the State. It will be seen that thus we compel these large forest areas to contribute to local improvements throughout the State.

PROFESSOR BULLOCK (Massachusetts): There are two subjects that have been touched upon this afternoon about which I am constrained to say just a word or two before the discussion is closed. One is the question of the separation of state and local revenue, and the other the matter of local option.

On the first topic, the separation of state and local revenue, those of you who are familiar with the development of the subject will be aware that the advocates of separation have lately discovered that it is necessary, after you separate your state revenue, to provide your state government with an elastic state revenue system. Otherwise, there can be no proper regulation of the expenditures of the revenue of the State. That was something that was overlooked in the early propositions for the separation of state and local revenues.

I wish to speak a few minutes as to the suggestions that have been made this afternoon for supplying that elastic revenue system. One of the suggestions is that the State should accumulate a surplus which should be applied to supplying the deficiency, and if proving greater than needed for that purpose, should be distributed among the local communities. I don't know how it may be in other States, but I am familiar with the history of the financial policy of Massachusetts and with the methods of our legislatures, and I am very certain that it would be undesirable for us to undertake to maintain a surplus in that way. I feel assured from what the gentleman from Pennsylvania said that Pennsylvania has found it very inconvenient to accumulate a surplus of several millions of dollars. Such a surplus accumulated and held in our State would tend to extravagant expenditure, and the practical result would be that the amount distributed to the various local communities in aid of local expenditures would very shortly be a minus quantity.

In the next place, it has been suggested that the State can vary rates on its taxes. In Massachusetts we have no state tax on which we can vary the rate. Those rates cannot be varied to suit the needs of our state government.

The habitation tax has been suggested, and whatever the merits of that tax, the habitation tax has never had and never will have the ghost of a chance of adoption in Massachusetts. We have an income tax, and collect therefrom perhaps some forty or fifty thousand dollars a year, and no State in this Union that levies an income tax has ever collected more. We have not been particularly successful, but we have been as conspicuously so as any other State that has experimented with the income tax, and you will see that an income tax producing that magnificent sum is not calculated to produce much of a surplus. There are no other taxes that can be suggested upon which the rates can be varied. Now it is said, retain then the practice of making a general assessment upon your town, but apportion that tax according to the amount raised by the local community for purposes of local taxation. I wish to call the attention of the Conference to the fact that that means the levying of state taxes, not upon the basis of the town which contributes, but upon the basis of the necessities of various

towns. We have some towns (I have in mind also several of our cities) that are so situated that from the very nature of the case they must, in order to maintain decent government, in order to get the same service that other cities get, spend from 25 to 50 per cent more in order to secure the same results, and to assess those towns with an extra portion of the state tax on account of their situation, is a proposition which, while it may be good in other States, would never in Massachusetts have the slightest chance. In the second place, that tax would be apportioned not only according to the necessities of the least favorably situated towns, but it would put upon the progressive towns and cities a great burden; upon those communities it would put a tax for their very progressiveness, which would mean that a city which wanted to raise the pay of its teachers, or introduce a pension system for them, or a system of manual training, or establish a manual training high school, or adopt any of the educational systems in any of the various ways in which we are finding it necessary to improve our educational system — why, that progressive town would be fined, would be taxed for that. On that account, in the State of Massachusetts it is practically certain that we should never apportion our state taxes upon the basis that will put a fine upon progress and put a tax upon the misfortune and the necessities of the less prosperous towns and cities of the State. So much for the matter of establishing an elastic system of the revenue with a complete separation of state and local taxes. Now, while I do not believe in a complete separation of state and local taxes, I believe that a light state tax is a desirable thing as a check upon the growth of expenditure and as a means of maintaining the budgetary equilibrium from year to year. We do not think it is desirable that our State should raise a great part of its revenues in other ways to make the state tax as light as possible. For a dozen or fifteen years our state tax has not exceeded \$1,500,000. Of that sum, substantially one half was assessed upon polls, and the various towns and cities levied upon property. We assessed upon property not more than \$750,000. Now, whereas the total tax levied upon property throughout the State at that time aggregated some fifty millions, the state tax levied upon

property did not amount to more than $1\frac{1}{2}$ per cent on the total property in Massachusetts. Such a low tax did not give to the local communities an excessive inducement to undervalue real property for the purpose of reducing their share of the state tax. Through the good offices of our tax commissioner — we have no State Board of Equalization — and through the fact that our state fund retained a comparatively small part of the total tax falling upon property in Massachusetts, it came about that real property is assessed so nearly, upon the average, at its true value that the United States Census in making an estimate of the true value of all the real property in Massachusetts took the assessed value of real property in Massachusetts and added thereto as a correction for any other assessment, not more than 10 per cent, which is the highest percentage, if I remember correctly, of the assessed value of property to the true value that will be found to exist in any other State.

Now in regard to the matter of local option, just one more word. Of course, local option in selecting sources of revenue has certain advantages. It is possible to see what some of those advantages are. Among the possible advantages would be that it would make it very easy for those localities to introduce the single tax. We can see that at once. Those of us who favor single tax naturally would favor local option. Those of us who do not favor the single tax have very good reason to scrutinize that proposition with extreme care, before we commit ourselves to it. I am not going to undertake to argue here the question of the single tax. I will simply state that I do not discuss this proposition from the viewpoint of a single taxer. I am not a believer in the single tax. Now from that viewpoint I understand that it is highly improper to grant local option to our communities in the taxing of many kinds of property, or taxation of business, and so far as I am familiar with the tax systems of other countries, I know of no country in the world in which such freedom is granted. In the kingdom of Prussia there is a practical illustration, and it is true that they have to a very high degree a separation of the sources of state and local revenues. In 1893, in the kingdom of Prussia, the State surrendered to the local community the tax on land, on

buildings and the tax on business. Land and buildings and business are no longer taxed for state purposes, and the localities are allowed, or are required to levy, a very large proportion of their taxes upon land, buildings and business; but when the State did that, it was very careful to retain in its own hands the assessment of property for taxation. The assessment of land and buildings and business is made by a body of assessors in order to secure uniformity, and the kingdom of Prussia takes no chances in regard to it, or in the matter of running the risk of lack of uniformity in the assessment of business. A system like that might work in a State like Massachusetts with reference to one single item, namely, the item of machinery. There is perhaps no State in the Union where machinery is taxed more heavily than in Massachusetts. It is proposed to exempt machinery. Some of the cities would be unable to exempt machinery under penalty of facing a practical bankruptcy if they undertook to do so. We have other cities which to-day are not prominently manufacturing centers, which collect a comparatively small amount of revenue from machinery, and they could without serious loss exempt machinery, and doubtless many of them would do so in order to attract manufacturing enterprises. Then what would happen? As a result of the lack of uniformity we would have a condition which would greatly effect a redistribution and rearrangement of the manufacturing industries of Massachusetts, from towns which from their necessities could not exempt machinery into towns which from a more favorable situation could and would exempt machinery. I do not want to weary you with the discussion of these points; I am not now undertaking to say what it may be inexpedient for other cities to do; I can only give you my personal opinion, discussing the matter of machinery from the point of view of Massachusetts.

I wish to agree thoroughly with what Professor Adams has said, and in the proposition to grant local option, full freedom of choice, or very large freedom of choice, in the exemption of property from taxation.

MR. POWERS (Washington, D.C.): I wish to call your attention to one agency that is found in government that may emphasize that fact, and it is this: We have the value of tax

commissions in States like Massachusetts emphasized by the facts which Professor Bullock has called to your attention, that in that State through the tax commission and the small state tax it has brought an equality, or rather a practical balance, to the assessment of valuations throughout the State and the apprehension of the true value. That is one value of an intelligently guided state commission. The state commissions are showing their value with reference to a great many other sources as well. If you will go over to the state house in this State, and examine the operation of the supervision of local accounts to find what has been done in this State in eliminating evils of local government and bringing order out of chaos, the chaos that comes from inefficient officials that may be elected, you will find something that is of value in government, showing that there are things in which we want a supervision of local authority by the State. The same principle is extending over this country, a movement for the extension of the supervision of local accounts by state authority; that has been and is saving to this State of Ohio thousands upon thousands of dollars, running up into the hundreds of thousands at the present time. You will find the same thing in the application of the independent Tax Commission Act, which has had very much to do with guiding, instructing and helping the local authorities. (*Applause.*)

MR. GILSON (Wisconsin): I wish to say in regard to the matter of the separation of state and local revenues that Wisconsin has practically reached that condition, and the state of the law is such, I think, that we are able to preserve such separation in a proper way. The revenues of Wisconsin for the support of the state government are derived from the taxes upon corporations, fees upon insurance and upon other subjects of like nature. We also levy in that State what is called a school tax of seven tenths of a mill. This tax is apportioned to the counties in the proportion of the assessed valuation in the county. The tax, when collected, is distributed back to the localities according to the school population. We also levy a tax of two sevenths of a mill for the support of the university. The school tax amounts to \$1,600,000; the university tax, approximately, to \$650,000. We have a provision in our law which

permits the Governor, the Secretary of State and the State Treasurer, when they ascertain, before the state levy, that the amount of money is sufficient, to appropriate the money in reduction of the school tax or the university tax. So that I think we have the machinery which will automatically preserve the separation of state and local taxation. If there is a surplus accumulated, it can be set aside for the support of schools and the university. If there is a deficiency or not enough money in the treasury to meet those needs, then a state tax may be levied.

EIGHTH SESSION

HELD IN THE ASSEMBLY ROOM OF THE PUBLIC LIBRARY, COLUMBUS,
THURSDAY EVENING, NOVEMBER 14, 1907, 7.30 TO 10 O'CLOCK

CHAIRMAN, GOVERNOR GUILD OF MASSACHUSETTS

PROGRAM

1. TAXATION OF LIFE AND FIRE INSURANCE CORPORATIONS.
Professor Solomon S. Huebner, University of Pennsylvania,
Philadelphia, Pa.
2. TAXATION OF COMPETITIVE INDUSTRIAL CORPORATIONS.
Hon. Theodore Sutro, Attorney, Chairman Committee on
Taxation, American Bar Association, New York City.
3. TAXATION OF PUBLIC SERVICE CORPORATIONS.
Professor Adam Shortt, Queens University, Kingston,
Ontario; Member of Tax Commission, Province of
Ontario, Canada.
4. TAXATION OF PUBLIC SERVICE CORPORATIONS.
Professor Carl C. Plehn, Professor of Finance and Statis-
tics, University of California, Berkeley, Cal.; Expert on
Taxation and Public Finance, State of California Com-
mission on Revenue and Taxation.
5. SPECIAL FRANCHISE TAXATION IN NEW YORK.
George S. Coleman, Assistant Corporation Counsel City
of New York, Hall of Records, New York City.
6. RELATION OF FRANCHISE TAXATION TO SERVICE RATES.
Allen Ripley Foote, President National Tax Association,
Commissioner Ohio State Board of Commerce, Colum-
bus, Ohio.
7. REPORT OF COMMITTEE IN RESOLUTIONS AND CON-
CLUSIONS.

THE TAXATION OF LIFE AND FIRE INSURANCE COMPANIES

BY PROFESSOR SOLOMON S. HUEBNER

University of Pennsylvania, Philadelphia, Pa.

OWING to the widespread ignorance of the annual level premium plan in life insurance, the utmost confusion exists to-day in the taxation of life insurance companies doing business in the United States. The vast accumulation of funds by the companies has given the impression that they were growing enormously wealthy; and legislators, failing either to understand the nature of these funds or appreciating the ease with which such funds could be reached by the tax collector, began to impose burdensome taxes upon the same. The result has been a confused mass of legislation and a great variety of taxes. About two thirds of the States tax the gross premiums received by the companies within the State, while several States tax the gross premiums of their home companies, no matter where collected. Some States tax the gross premiums after deducting losses and commissions, while a few States tax the net assets or the surplus of the companies in one form or another. In addition to these taxes there is an endless variety of charges for filing charters, annual statements and other papers, and for licensing agents, valuing policies, covering the expenses of the commissioner of insurance, etc. To make matters worse some States permit their municipalities to impose taxes upon the companies, while others provide for retaliatory legislation so that they may do to the other fellow what he is doing to them. In practically every State the insurance department is more than self-sustaining by virtue of the fees received.

The combined effect of this multitude of taxes and fees is an annual charge upon the life insurance companies of approximately \$12,000,000. This large amount is levied without any approximation toward equality between the different States.

Thus, taking the New York Insurance Company as an illustration, it appears from a recent computation that 90 per cent of all the taxes paid by this large company were paid in States and Territories having less than 50 per cent of the business. The taxes paid by this company for the mere privilege of doing business exceeded the total salaries of officers and employees at the home office of the company.

THE TAXATION OF LIFE INSURANCE ASSETS

Turning to the taxation of the assets of life insurance companies, one of the two plans most generally adopted by the States, we find that many prominent life insurance underwriters have attempted to arouse a sentimental feeling against the tax, since they regard life insurance assets as a most beneficent provision against loss occasioned by the unexpected termination of earning power, and thus of invaluable service to the State in reducing the number of those who would become public charges. While there is much weight to this argument, and while it has received full recognition in certain European countries, there is another objection against the taxation of life insurance assets, an objection, however, which applies to many other taxes in this country besides life insurance taxation. The assets of life insurance companies consist almost entirely of first mortgages, bonds and stocks, that is to say, evidences of wealth which have already been reached by the tax collector, and which would be taxed a second time, and in many cases even three times, if the state laws providing for the taxation of life insurance assets be carried out. While many of the problems connected with double taxation are well-nigh insolvable, there is a growing conviction that double taxation in the various States can only be obviated by having the States give up the plan of taxing both wealth and the evidence of ownership in that wealth.

The bearing of this plan upon the taxation of life insurance companies is well brought out by Dr. Lester W. Zartman in his recent book on "The Investments of Life Insurance Companies":

"If the States would tax corporations upon their wealth where it is located," he writes, "and not attempt to tax the multitude

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of holders of corporation securities, and would tax real estate and not the mortgage upon it, if all this were done, then insurance assets would not be taxed, for they consist, as we have seen, of mortgages, bonds and stocks. Thus if the above principle of taxation were adopted, the problem of taxing insurance companies upon their assets would be solved. The objection to taxing these assets is not that they belong to companies which have the worthy object of relieving distress, but that such a tax should not be levied on the kind of assets which they possess, no matter to whom they belong.

"Not only does the taxation of insurance assets by the State where the company is located result in much double taxation, but it is peculiarly unjust as it levies a tax on wealth which is without the State and owned by citizens without the State. No successful insurance company has gathered its assets even for the most part from the savings of citizens within the State where it is located, savings have flowed into it from every part of the country, these to be held, invested and accumulated at interest, and yet the State in which the company is located claims the right to tax all these savings even if they do belong to citizens without the State. An insurance company must have a habitat in some State, but the fact that some one State is fortunate enough to have a successful company established within its boundaries does not give it the moral right to tax all the assets which that company possesses. If these States with companies doing business throughout the country are going to continue the taxation of property rights of persons, and thus those possessed by their insurance companies, they should be consistent at least and tax only that portion of the assets which belong to citizens of their States, leaving to other States the right to do as they please with the portions belonging to their citizens, but which for the time being happens to be stored away in the vaults of the home office in another State."

THE TAXATION OF LIFE INSURANCE PREMIUMS

As already explained, most of the States levy taxes upon the gross or net premiums collected within their boundaries by outside companies. Some years ago States began taxing their home companies upon their assets, but to protect these companies against any evil effects of the tax in the competition with foreign companies, these States began to tax the premiums collected within the State by outside companies. As soon as one State began to tax the premiums collected by the companies of another State, that State at once retaliated by taxing

the premiums collected by the companies of the first State. Other States, although having no companies of their own, appreciated the revenue-getting possibilities of the premium tax, and promptly followed the example of their neighbors. Furthermore, most life insurance companies were domiciled in the Eastern States which attempted to secure the accumulations of their companies, as far as possible, for home investments. Western States, however, required much capital at this time, and thus regarded with great disfavor the apparent loss of capital through the collection of premiums by Eastern companies, and attempted to establish home companies by levying heavy taxes on outside companies; hence the general introduction and popularity of the tax on life insurance premiums.

The tax on premiums may be objected to on practically the same ground as the tax on life insurance assets. Premium taxes are usually supported on the theory that since a man who invests his money in bonds or stocks is usually taxed, the premium which a person devotes to the buying of life insurance should also be taxed. As regards endowment policies, considerable weight must be given to this contention. But if it is the desire of the several States to avoid double taxation as much as possible and to tax wealth where it is located rather than the evidences of the ownership of that wealth, then it must be admitted that neither the investor in securities nor the investor in life insurance should be taxed. The investor in stocks and bonds should be taxed but once, *i.e.* through a corporation tax, while the buyer of life insurance should also be taxed in the same manner, since life insurance assets, as we have already seen, also consist of stocks, bonds and other evidences of ownership of wealth.

But even if the State does decide to tax premiums, it does not follow that this tax should be collected from the insurance companies. Life insurance is based upon a mathematical calculation involving an assumed rate of death and an assumed rate of interest on the assets of the company, usually 3 or 3½ per cent. In other words, a life insurance company enters into a fixed contract with the policy holders, a contract which is unilateral in character and which can under no conditions be terminated by

the company. The annual premium is fixed when the contract is first entered into and remains the same for life, without any possibility of being increased to meet the needs of the company. Increased taxation upon the premiums of the company after the policy has been issued might, therefore, prove a serious burden upon the company, since life insurance companies cannot possibly terminate their contracts and in that way avoid the tax. If a premium tax is to be levied, the companies ought to be given the right to increase their premiums proportionately to the tax; or a better plan still would be to impose the premium tax directly upon the policy holder.

We must conclude, therefore, that the taxation of life insurance assets or life insurance premiums is wrong in principle and very conducive to heavy taxation as well as double taxation. But this does not mean that life insurance companies should escape all taxation. It is generally conceded that life insurance companies ought to pay a tax upon their real estate just as in the case of private individuals, but this tax ought to be imposed where the property is located and not taxed twice, as is done by some States with their home companies. Furthermore, if the life insurance business of any company is conducted upon the stock plan, it is only just that the State should tax the capital stock or the dividends upon the stock in just the same manner as other capital stock is taxed. If any other taxation is deemed necessary, it seems to me that the best interests of all would be conserved if the taxes were levied upon the dividends paid by companies upon their policies. Such a tax would be upon the profits of the company, upon the amount of money earned over and above what is needed to pay maturing obligations.

A POLICY OF LENIENCY TOWARD LIFE INSURANCE COMPANIES IS DESIRABLE

In revising the present system of taxing life insurance companies along the lines suggested it is highly important that our state legislatures should weigh carefully the beneficent features of insurance against death. Life insurance is not a business which should be penalized with repressive measures, but its continuance and spread throughout the width of the land should be fostered. Its beneficent influence should be felt in every

home just like the influence of the public school and the church. The vast accumulation of the companies must not be regarded as surplus or profit, but as money *held in trust* by them for millions of people who have contributed their savings to a common fund in order to provide mutual protection against the inevitable loss occasioned by death. This trust fund must be returned to the policy holders when death occurs. Nearly all life insurance is to-day conducted by mutual companies which are not organized for profit, but for insurance against the inevitable event of death. By accumulating the savings of millions and carefully protecting this huge trust fund by judiciously investing it in first mortgages or low interest-bearing, gilt-edge securities, the companies render a great service to the State by vastly reducing the amount which would have to be expended by the State for those who would become a public charge. Instead, therefore, of taxing these assets to the extent of millions annually, the State ought to treat the life insurance business with leniency. Encouragement and not repression should be the keynote of our tax system as applied to life insurance companies. At this point I can do no better than quote an admirable extract from an address delivered before the classes in insurance at the University of Pennsylvania by Mr. J. W. Hamer, manager of the loan department of the Penn Mutual Life Insurance Company. He said:

“Under an intelligent system of taxation, the tax is placed upon the profit; you do not tax a loss. In the purely mutual company, there’s no such word as profit; the company performs its function with no such object; insurance is furnished at its actual cost. The theory which underlies the formation of a purely mutual life insurance company is that it is simply a means for the equal distribution of an inevitable loss. Let us suppose a combination of ten, one hundred or one hundred thousand men—the number has no significance except to produce an average—let us suppose each of these men agrees to pay a certain sum for the relief of the families of those who die—to restore to each family that of which it has been deprived, the insurable value of its departed head. Elaborate it, complicate it with varied forms of policies, safeguard it with actuarial tables as you will, and still the basic fact remains, beyond dispute, that each member of a mutual company, by payment of his premium, merely contributes that sum which represents his share of loss. Taxation of this, is so much added to the loss, or so much sub-

tracted from the insurance benefit. It is difficult to understand the justice, the wisdom or even the expediency of putting a tax upon a loss and thus adding to its burden. Whatever the original intent, the ultimate result of the formation of a mutual company is to prevent the families of its members from becoming a charge upon the public. Every dollar of tax upon a mutual company, therefore, antagonizes public welfare, in so far as it tends toward the defeat of this beneficent result."

In striking contrast to the unscientific and heavy taxation of life insurance companies in America, may be mentioned the fair treatment of the business by European countries. Instead of taxing the premiums, as is so generally the case here, England not only does not tax such premiums at all, but offers a special inducement to its citizens to devote a considerable portion of their income to the purchase of life insurance. Every policy holder whose income is large enough to come within the provisions of the income tax is permitted, in making his income return to the government, to deduct life insurance premiums to the extent of one sixth of his income. The companies themselves must pay the income tax on investments, but this tax does not constitute a second tax upon the assets of the company, since it corresponds to the corporation tax prevailing in this country. Holland in its tax upon capital especially favors life insurance by exempting life policies from taxation. Furthermore, as in England, the income tax law in Holland permits every policy holder liable to the tax to deduct insurance premiums to the extent of \$40 from the income declared to the government. The treatment accorded to life insurance in these countries shows a proper understanding of the fundamental character of this form of insurance and reflects the progress which Europe is making in solving the whole complex problem of taxation.

THE TAXATION OF FIRE INSURANCE COMPANIES

Turning to the taxation of fire insurance companies, we find just as much lack of uniformity and inequality of taxation among the several States as now prevails in the taxation of life insurance companies. The tax is usually on the gross premiums of the company, and amounts on the average to over 2½ per cent. In

other words, fire insurance companies are taxed on their sales of the commodity, insurance, irrespective of the profit or loss upon the business, i.e. the taxes upon fire insurance companies in this country are generally levied according to a method which, if extended to other business pursuits, would imply taxing merchants 2½ per cent upon their sales.

While the tax on gross premiums is the most expedient method available to the States to collect the most revenue from the company with the least amount of trouble on the part of the tax collector and the smallest possibility of evasion on the part of the taxed, the injustice and hardship of the gross premium tax to both insurer and insured has too often been demonstrated. Fire insurance, unlike life insurance, is not mathematically scientific. The constant changes in the methods of construction of buildings and processes of production combined with the highly competitive character of the business and the constantly recurring conflagrations, make fire insurance one of the most hazardous of great commercial pursuits. Let it not be forgotten that during the quarter century following 1878 \$44,408,000 of capital has been forced out of the fire insurance business as compared with the \$56,102,875 of capital employed at a recent date by the one hundred and forty-seven American and foreign joint stock companies reporting to the New York insurance department.

The explanation for this unstable character of fire insurance capital is found in the peculiar condition surrounding the business. Fire insurance is a business which is not based on constant factors, but which must constantly adapt itself to new conditions over which it has no control. An intelligent system of taxation requires that the tax be placed upon the profit of a business and not upon the losses. It seems especially fitting, therefore, that the method of taxing fire insurance companies should be so devised as to reach the profit of a company after making allowance for losses and proper expenses. No good reason can be offered for taxing companies on the gross premiums received in any State, where such premiums are exceeded by the sum paid to the citizens of that State in the shape of fire losses and agents' commission. It has frequently happened that the total premium income of the fire insurance companies of this

country has been exceeded by the outgo for losses and expenses, which fact, as has been so aptly stated, means "that in a State in which the business has been unprofitable, the company actually pays a tax for the privilege of leaving more money in the State than it takes out of it, and so for the privilege of making a loss." The period from 1888 to 1897 may be cited as an illustration. Five of those years (1889, 1891, 1892, 1893 and 1898), according to an analysis by Mr. F. C. Moore, show a loss in the total business of fire insurance companies amounting to \$53,296,021, yet the taxes paid by the companies to the several States during these years aggregate \$14,554,941. The years 1891 and 1893 proved extremely unprofitable, showing a loss respectively of \$9,218,797 and \$10,410,102, but the taxes paid amounted nevertheless to \$2,596,902 and \$2,961,571. The remaining six years of the period show a net gain (that is to say, an excess of premiums over losses). But a comparison of the taxes paid during these years with the net premium income reveals a tax burden on the fire insurance business which is truly astonishing, and probably not to be found in any other business. The ratio of taxes to net gain for these years varies from a minimum of 25.38 per cent in the year 1895 to 36.45 per cent in 1897, 88.49 per cent in 1890 and 323.69 per cent in 1882. Later data have been furnished by Mr. Richard N. Bissell in a lecture before Yale University. "The net profit for all companies," he calculates, "for the decade from 1891 to 1902, disregarding the increase for outstanding liabilities, was \$59,571,933. The taxes paid during the same period amounted to \$40,428,927. The premiums, roughly speaking, were \$1,500,000,000; therefore, the taxes collected during these years were equal to $2\frac{7}{10}$ per cent of the entire amount of premium, and $68\frac{1}{5}$ per cent of the entire profit resulting from their insurance transactions."

To continue taxing premiums without reference to the profitability or unprofitability of the business must inevitably result in increased rates to property owners, since insurance companies must pay losses and expenses out of gross premiums. A tax on profits, however, *i.e.* a tax on the premium receipts collected in a State after deducting at least the amount paid in the State for losses, is a tax the justice of which is universally recognized by fire underwriters and should, if made reasonable

in amount as compared with the taxes levied on other industries, be paid by the companies without complaint.

The attitude of fire underwriters toward the gross premium tax becomes very clear upon an examination of the "standard universal schedule for rating mercantile risks," the schedule used for rating mercantile risks in the larger cities of the East. Provision is actually made in this schedule (item 139 of the schedule) that in case state and municipal taxation of the companies is other than on the net results to the company after deducting losses and expenses and not exceeding 2 per cent thereon, an addition shall be made to the rate on risks in that locality according to the amount of such excess taxation. As a justification for this policy of adding to the insurance rates for excessive taxation and thus shifting the tax to the property owner, the following suggestive and instructive explanation is offered in the schedule: "This schedule is based upon a 5 per cent profit above the actual cost of insuring property, and contemplates no tax other than that explained under item 139 above. Of course, if a further tax is imposed, the expenses of the companies will be to that extent increased as an extra premium must be collected. Insurance companies do not object to paying to any State a percentage tax on the profits of their business in the State, or upon the excess of their received premiums over paid losses and expenses. It is difficult for them to see why they should be called on to pay a tax on the gross premiums collected in any State where the amount paid by them to the citizens in the shape of fire losses and commissions to agents, who are resident citizens, may consume all or more than the premiums received. In such case they are taxed for the doubtful privilege of leaving more money in the State than they take out of it."

TAXATION OF COMPETITIVE INDUSTRIAL CORPORATIONS

BY HON. THEODORE SUTRO

Of the New York Bar, Chairman Committee on Taxation, American Bar
Association, Former Commissioner of Taxes, City of New York

ONE of the planks in the platform of principles of the National Tax Association is that "property shall be so classified that every tax shall bear equally on all persons similarly situated."

Based upon this principle, the question naturally arises, with reference to the subject of this paper, Why should persons engaged in similar pursuits, whether as individuals or as corporations, be subjected to wholly unequal burdens of taxation, as in practice is found to be the case? Corporations are creations of the government, and if the government conferred upon them such extraordinary privileges that, in consequence thereof, the opportunities for the profitable transaction of their business were vastly superior to those of individuals, it might well be argued that they should also make a proportionately larger contribution, in the way of taxes, to the support of that government. The privileges thus enjoyed by corporations, as distinguished from a copartnership, are, in fact, however, chiefly the following: A longer or practically unlimited existence, for the reason that neither death nor an act of bankruptcy on the part of any of its members dissolves the corporation; that the financial liability of its individual members is limited, and that new members may be added, simply by the transfer of its shares, without either terminating or jeopardizing its integral existence. Possibly, also, through such power of disposing of its shares of stock, it may more readily raise capital than individuals; yet that does not by any means always follow, and in treating the subject of taxation from the point of view that its burdens should "bear equally on all persons similarly situated," the privileges thus enjoyed by corporations, as such, are not suffi-

cient to justify any such discrimination against them, as now exists, in contradistinction from individuals or firms in the same line of business. We find, in fact, that also some of the largest business concerns in the world are not of a corporate, but of an individual or copartnership character, and the conveniences enjoyed by corporations, above enumerated, are certainly not sufficient to impose upon them burdens of taxation so much greater than, as will hereinafter appear, are imposed upon individuals or copartnership business concerns.

In considering this subject I speak, of course, exclusively of the corporations embraced within the title of this paper "industrial" corporations. Where the State confers some especial privileges upon corporations, such as public franchises or utilities, an entirely different situation is presented; and as, through such franchises, an extraordinary privilege, in which the public is greatly interested, is created in their favor in contradistinction from individuals, such corporations should also, properly, be compelled to pay some exceptional tribute to the State by way of compensation in the shape of taxes.

That it is to the interest of the State that manufacturing, agriculture and the distribution of merchandise generally within its borders should be encouraged to the utmost, requires no argument; and as it must be conceded that by far the greater amount of such business is now in the hands of corporations, it is also to the interest of the State to facilitate and not impede by undue discrimination the machinery through which these industrial pursuits are now mainly carried on. Where one hundred years ago industrial corporations were hardly known, and all the business of the world was in the hands of individuals or firms, statistics show that quite the contrary is now the case. In Moody's Manual for the year 1907 the number of "active, operating, industrial or miscellaneous corporations" in the United States reporting to that publication is given as 1466, with a capital stock in the aggregate of \$7,585,340,000, exclusive of all mining corporations, except iron and coal mining corporations. These figures do not embrace so-called "close" corporations, the number of which is legion and their aggregate capitalization incalculable. According to Dr. John P. Davis, in his work on the "Origin and Development of Corporations" (1904),

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ONE of the planks in the platform of principles of the National Tax Association is that "property shall be so classified that every tax shall bear equally on all persons similarly situated."

Based upon this principle, the question naturally arises, with reference to the subject of this paper, Why should persons engaged in similar pursuits, whether as individuals or as corporations, be subjected to wholly unequal burdens of taxation, as in practice is found to be the case? Corporations are creations of the government, and if the government conferred upon them such extraordinary privileges that, in consequence thereof, the opportunities for the profitable transaction of their business were vastly superior to those of individuals, it might well be argued that they should also make a proportionately larger contribution, in the way of taxes, to the support of that government. The privileges thus enjoyed by corporations, as distinguished from a copartnership, are, in fact, however, chiefly the following: A longer or practically unlimited existence, for the reason that neither death nor an act of bankruptcy on the part of any of its members dissolves the corporation; that the financial liability of its individual members is limited, and that new members may be added, simply by the transfer of its shares, without either terminating or jeopardizing its integral existence. Possibly, also, through such power of disposing of its shares of stock, it may more readily raise capital than individuals; yet that does not by any means always follow, and in treating the subject of taxation from the point of view that its burdens should "bear equally on all persons similarly situated," the privileges thus enjoyed by corporations, as such, are not suffi-

New York, and together employ in their business the same amount of capital which is employed by the said corporation.

The share capital of the corporation is \$600,000, which is unimpaired, as its net assets fully equal that amount. Immediately upon incorporation this company had to pay an organization tax to the State of New York of one twentieth of 1 per cent of its proposed capital of \$600,000, that is to say, \$300, in addition to fees for filing its papers in the offices designated by law for that purpose. This organization tax and these fees constitute, however, the smallest portion of the burden imposed upon it by the State. In addition thereto, the State exacts an annual, continuing tax from the company, being a domestic corporation, based upon a valuation of its capital employed within the State. As a result of numerous conflicting decisions of the courts, it has at last been settled that this company must pay to the State a tax not only on all its tangible property in that State, such as real estate, merchandise, material, machinery, furniture and fixtures, but upon all its moneys wherever deposited, within or without the State; upon its accounts and bills receivable from wherever owing if resulting from sales made from its New York office; and, in addition thereto, also upon a valuation of patent rights, trade marks, copyrights and good will, so called, which it may own, in the proportion of what the capital employed in the State of New York bears to its entire capital. This capital thus held to be employed in the State of New York, amounting to \$150,000 of real estate and to \$300,000 of other assets, together \$450,000, is under the present law of that State subject to an *annual* tax of about \$675 if the company pays an annual dividend of 6 per cent, and proportionately greater if the company pays a larger dividend.

In the foregoing I have summarized what the company has to pay in the way of tribute merely to the State, from which the competing business referred to, carried on by individuals, is wholly exempt.

With reference to local taxation the situation of the company is as follows:

In the city of New York it occupies its own building, which is assessed for taxation at \$100,000, the taxes on which, at

the current rate of \$1.50 per \$100, result in a tax bill of about \$1500. Let us assume that this assessment of \$100,000 on the company's real estate is about two thirds of its actual value, that is to say, of \$150,000, at which last-mentioned figure the company also carries the said real estate on its books. In the varying and unsystematized method of assessing real estate in New York it is an open secret that assessments are at various percentages of market value, all the way from 50 per cent to 85 per cent. It is therefore not an unreasonable assumption that the assessment of \$100,000 on its real estate represents an actual value of \$150,000. The competing individual firm owns a similar piece of real estate for its business purposes and is assessed similarly, and the amount of tax which such firm has to pay at the current rate amounts to \$1500 per annum. With reference to the company, however, by way of penalty, as it were, for being a corporation, the following method is pursued: Because it carries the real estate on its books at \$150,000, and is disinclined to place its value at a less sum under oath, the full sum of \$150,000 is included as an asset among its other assets, and an allowance made of the assessed valuation of \$100,000; so that, in contradistinction from the individual, the company's real estate is assessed at the full sum of \$150,000, as against an assessment of the real estate of the individual of \$100,000, creating an excess as against the corporation of \$50,000, which at the current rate of \$1.50 per \$100, subjects it to the payment of an additional tax bill of \$750, or a total of \$2250, as against a tax bill of \$1500 against the individual.

With reference to its other assets they are held to include not only those already enumerated as taxable for state purposes (except patents, copyrights, trade marks and good will), but, in addition, all accounts and bills receivable owing to the company, not only from sales made from its office in the State of New York, but from any of its agencies in other States. For local purposes the total assessment against the company, exclusive of the tax specifically falling on its real estate, is again fixed at \$300,000, the same as for state purposes, because the inclusion of certain assets for local purposes, which are not included in the assessment for state purposes, about counter-

other words, fire insurance companies are taxed on their sales of the commodity, insurance, irrespective of the profit or loss upon the business, i.e. the taxes upon fire insurance companies in this country are generally levied according to a method which, if extended to other business pursuits, would imply taxing merchants 2½ per cent upon their sales.

While the tax on gross premiums is the most expedient method available to the States to collect the most revenue from the company with the least amount of trouble on the part of the tax collector and the smallest possibility of evasion on the part of the taxed, the injustice and hardship of the gross premium tax to both insurer and insured has too often been demonstrated. Fire insurance, unlike life insurance, is not mathematically scientific. The constant changes in the methods of construction of buildings and processes of production combined with the highly competitive character of the business and the constantly recurring conflagrations, make fire insurance one of the most hazardous of great commercial pursuits. Let it not be forgotten that during the quarter century following 1878 \$44,408,000 of capital has been forced out of the fire insurance business as compared with the \$56,102,875 of capital employed at a recent date by the one hundred and forty-seven American and foreign joint stock companies reporting to the New York insurance department.

The explanation for this unstable character of fire insurance capital is found in the peculiar condition surrounding the business. Fire insurance is a business which is not based on constant factors, but which must constantly adapt itself to new conditions over which it has no control. An intelligent system of taxation requires that the tax be placed upon the profit of a business and not upon the losses. It seems especially fitting, therefore, that the method of taxing fire insurance companies should be so devised as to reach the profit of a company after making allowance for losses and proper expenses. No good reason can be offered for taxing companies on the gross premiums received in any State, where such premiums are exceeded by the sum paid to the citizens of that State in the shape of fire losses and agents' commission. It has frequently happened that the total premium income of the fire insurance companies of this

Should it on the other hand have, say, \$150,000 of assets in the State of New Jersey, and owe specifically against these assets \$50,000, that liability would not be taken into consideration, but the assessment made at the full sum of \$150,000.

In the State of Pennsylvania, in Philadelphia, the company has a business branch for the sale of its goods, the amount of capital employed there being the sum of \$50,000, consisting of merchandise, furniture and fixtures and cash in bank. Also in that State the company must, upon commencing to do business there, pay a bonus or license fee computed at the rate of three and one third mills per dollar, which on \$50,000 gives \$166.67. It also has to pay an *annual* tax on its assets (capital stock tax). In connection with these matters the company has to file various papers for which additional fees are exacted.

With reference to the specific example of the chemical company hereinbefore referred to, the matter therefore sums itself up about as follows:

In the State of New York, taxes imposed upon it for state purposes, about	\$675
In the city of New York, for local purposes . . .	6750
In New Jersey, for local purposes	2500
In Pennsylvania, for state and local purposes, of which \$250 is apportionable to state purposes . .	1000
Making a total <i>annually</i> of	<u>\$10,925</u>

which, as the company has never earned over a 6 per cent dividend on its share capital of \$600,000, that is to say, an annual dividend of \$36,000, is equivalent to an income tax of about 30 per cent.

In addition, on commencing business in the State of New York, it is subject to an organization tax of \$300; in New Jersey to a license tax of, say, \$100; and in Pennsylvania to a bonus or license tax of \$167, making an additional total of \$567.

On the other hand, the individual or firm engaged in the same line of business, whose members are residents of the city of New York, with the same total unimpaired capital of \$600,000, with the same branches and employing the same

the premiums collected by the companies of the first State. Other States, although having no companies of their own, appreciated the revenue-getting possibilities of the premium tax, and promptly followed the example of their neighbors. Furthermore, most life insurance companies were domiciled in the Eastern States which attempted to secure the accumulations of their companies, as far as possible, for home investments. Western States, however, required much capital at this time, and thus regarded with great disfavor the apparent loss of capital through the collection of premiums by Eastern companies, and attempted to establish home companies by levying heavy taxes on outside companies; hence the general introduction and popularity of the tax on life insurance premiums.

The tax on premiums may be objected to on practically the same ground as the tax on life insurance assets. Premium taxes are usually supported on the theory that since a man who invests his money in bonds or stocks is usually taxed, the premium which a person devotes to the buying of life insurance should also be taxed. As regards endowment policies, considerable weight must be given to this contention. But if it is the desire of the several States to avoid double taxation as much as possible and to tax wealth where it is located rather than the evidences of the ownership of that wealth, then it must be admitted that neither the investor in securities nor the investor in life insurance should be taxed. The investor in stocks and bonds should be taxed but once, *i.e.* through a corporation tax, while the buyer of life insurance should also be taxed in the same manner, since life insurance assets, as we have already seen, also consist of stocks, bonds and other evidences of ownership of wealth.

But even if the State does decide to tax premiums, it does not follow that this tax should be collected from the insurance companies. Life insurance is based upon a mathematical calculation involving an assumed rate of death and an assumed rate of interest on the assets of the company, usually 3 or 3½ per cent. In other words, a life insurance company enters into a fixed contract with the policy holders, a contract which is unilateral in character and which can under no conditions be terminated by

the company. The annual premium is fixed when the contract is first entered into and remains the same for life, without any possibility of being increased to meet the needs of the company. Increased taxation upon the premiums of the company after the policy has been issued might, therefore, prove a serious burden upon the company, since life insurance companies cannot possibly terminate their contracts and in that way avoid the tax. If a premium tax is to be levied, the companies ought to be given the right to increase their premiums proportionately to the tax; or a better plan still would be to impose the premium tax directly upon the policy holder.

We must conclude, therefore, that the taxation of life insurance assets or life insurance premiums is wrong in principle and very conducive to heavy taxation as well as double taxation. But this does not mean that life insurance companies should escape all taxation. It is generally conceded that life insurance companies ought to pay a tax upon their real estate just as in the case of private individuals, but this tax ought to be imposed where the property is located and not taxed twice, as is done by some States with their home companies. Furthermore, if the life insurance business of any company is conducted upon the stock plan, it is only just that the State should tax the capital stock or the dividends upon the stock in just the same manner as other capital stock is taxed. If any other taxation is deemed necessary, it seems to me that the best interests of all would be conserved if the taxes were levied upon the dividends paid by companies upon their policies. Such a tax would be upon the profits of the company, upon the amount of money earned over and above what is needed to pay maturing obligations.

A POLICY OF LENIENCY TOWARD LIFE INSURANCE COMPANIES IS DESIRABLE

In revising the present system of taxing life insurance companies along the lines suggested it is highly important that our state legislatures should weigh carefully the beneficent features of insurance against death. Life insurance is not a business which should be penalized with repressive measures, but its continuance and spread throughout the width of the land should be fostered. Its beneficent influence should be felt in every

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rule, altogether unreliable. The amount is merely a guess, which sometimes turns out to be right, but generally wrong. Even the system employed as against corporations preliminary to receiving their reports is utterly ridiculous, although somewhat more systematic than that employed as against individuals; all domestic corporations are assessed each year at the full value of their share capital, which it needs no argument to show is absurd, as share capital is no criterion at all of the actual net assets of a corporation, which alone are taxable for local purposes under the laws of the State of New York.

Fourth. Reformatory legislation is also required in those States, as, for example, in New York, where the method of taxing industrial corporations results in assessing their real estate holdings at full value, as distinguished from an assessment of the real estate of competing individuals at a sum considerably less than full value.

Fifth. Another matter requiring most careful consideration is what method should be adopted with respect to the assessment of such assets as moneys on deposit and bills and accounts receivable. The simplest way would be to assess these once for all in the State of their incorporation, and there to embrace all accounts and bills receivable, no matter from what sales they may arise, whether within or without that State.

Sixth. Shares of stock in the hands of individuals should be uniformly exempt from taxation, but all taxes should be directed only against a corporation as a unit, and with respect to this, perhaps, also every other paper evidence of an interest in corporate property should be taxed in the same way. In regard to this last-mentioned matter a resolution adopted by the National Conference on Taxation held under the auspices of the National Civic Federation at Buffalo in the month of May, 1901, strongly appeals to me as a probable solution, namely, "that the same property should not be taxed at the same time by two State jurisdictions, and to this end, that if the title deeds or other paper evidences of the ownership of property, or of an interest in property, are taxed, they shall be taxed at the *situs* of the property, and not elsewhere."

But, it may be asked, how is it that the carrying on of industrial pursuits has concentrated more and more in the hands of

corporations, if the burdens of taxation imposed upon them are so disproportionately greater than those imposed upon individuals in the same pursuit? My answer to this would be that whether an unequal burden of taxation does or does not injuriously affect a certain pursuit is not the question. The only question involved is whether there is any inequality in the measure imposing the burden. If that is so, then the principle is wrong upon which the tax law is founded and the tax law itself is wrong. Whatever may have been the practical or apparent effect in a given case, in the past, it will necessarily follow that eventually the baneful result of such an unjust measure must be felt and end in serious injury. Furthermore, the fact that the larger part of industrial business is now carried on by corporations does not at all argue that these corporations are uniformly prosperous. My own experience proves that numbers of them are struggling on, simply to maintain their business, in the hope that at some time in the future a turn for the better may come, and with these the unequal burden of taxation imposed upon them is a real hardship. It is furthermore true, within my own experience, that many corporations by reason of these unequal burdens have been driven to dissolve their corporate existence and again merge into an individual or copartnership business. Lastly, the policy of a wise legislator must not be to wait until an injury has been done beyond repair, through vicious legislation, but rather to forestall the happening of such an unfortunate event. The object of this Conference is to consider what measures should be adopted to obtain such uniformity of legislation in all the States that it may best insure the greatest benefit for the greatest number at the same time that a sufficient revenue will be obtained for the support of the government; and if, as already stated, it is to the interest of the State to encourage production of every kind, whether by manufacture, agriculture or otherwise, it needs no further argument to enforce the correctness of the principle that, whatever may be the extent and resources of industrial corporations at the present time, all measures must be avoided which may tend to retard, instead of furthering, their still greater prosperity.

The State is no more justified in imposing exceptional burdens,

through unequal tax laws, upon the very agencies which are best adapted to further its prosperity, such as industrial corporations, than it would be in imposing a penalty or fine upon other like agencies, instead of holding out special inducements and rewards to them; as it does, for example, in issuing letters patent to or securing through copyrights and trademarks those persons who are engaged in pursuits that especially tend to benefit the country. I have already pointed out that the advantages resulting from the incorporation of industrial enterprises are by no means of an extraordinary nature, so that corporations such as these are practically on the same plane as individuals. From the point of view of a high order of statesmanship it would, therefore, not at all be out of the way if these industrial corporations, through which the wealth of our country has been and is being constantly developed, were actually encouraged and favored through some substantial privileges and rewards, rather than that the contrary policy should be pursued of constantly making war upon them and thinking out methods whereby they may be discriminated against, as if they were engaged in some nefarious pursuit, which ought, if possible, to be crushed out of existence.

And this leads me to say in conclusion that the hue and cry of demagogues, so popular at the present time in this country, directed against everything that bears the name of corporation, cannot be condemned in terms too strong. It only tends to inflame the masses, who do not give the subject any thought, at the same time that it works directly against the interest of these masses, in that it imposes upon them, as consumers, eventually the very burdens which their false leaders are anxious to have imposed upon the machinery, which has done and is doing the chief work in the creation of our national wealth. This indiscriminate warfare upon all corporate bodies, especially when directed against industrial corporations, because of some fancied advantage in the way of a monopoly or exclusive privilege which they are supposed to enjoy, is in fact in nearly all cases founded upon an utter misunderstanding of their actual situation.

This much I hope that I have at least made clear in the foregoing paper, viz.: Industrial corporations are certainly not

avored by the governmental authorities, as existing legislation is on the contrary specifically directed against them to their great disadvantage as compared with individuals. Instead, therefore, of clamoring for still more oppressive measures, the people ought to be made to understand that a contrary policy should be pursued, and that the bodies that are engaged in the business of fostering and multiplying the industries of this country should at least be placed upon a *par* with individuals who are endeavoring to do the same thing, though, by reason of the limitation of their resources, in a less efficient and therefore also less successful manner. Certainly the opposite proposition must be held true, beyond question, that there is no reason in the world why individuals engaged in industrial pursuits should be unduly *avored* as against corporate bodies, as is now the case; for, if it is to the interest of the country to encourage industrial pursuits to the utmost, then also the machinery, as already stated, which is best adapted to carry on and develop these industrial pursuits should be developed to the utmost, instead of being crippled through unjust discrimination, in subjecting it to undue and unequal burdens of taxation.

THE TAXATION OF PUBLIC SERVICE CORPORATIONS

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THE ordinary system of local taxation, both as to the needs to be supplied from the taxes collected, and as to the basis upon which the levies are made upon the contributors, is the natural and obvious outcome of a concrete situation dealt with in a practical manner. The situation is one in which the ordinary citizen has his permanent residence in one locality, where also practically all of his property is located or invested. If individuals sell produce abroad or import supplies from without, the exports and imports normally balance each other in concrete goods within a limited time. The public services required by the inhabitants, to furnish which is the occasion for the levying of taxes, are required by all the community, and are directly or indirectly in the interest of the citizens in fair proportion to their wealth. Substantial justice is maintained therefore by treating all property owners alike.

In many rural sections to-day, and for the majority of the citizens in our towns and villages, this principle may still apply. One need not touch upon all the intermediate stages in the development of property rights, in the forming of corporations, the creation of share capital and of mortgage bonds, with the facilities for their exchange, and the consequent wide diffusion and frequent shifting of ownership. But it is quite obvious that in dealing with such public service corporations as railways, steam or electric, telegraph, telephone and express companies, we have to deal with forms of property and phases of ownership which have little of the old relationship to locality, as regards the possession of property, and even less relation to the need for public service, which furnishes, on the one hand,

the local basis for taxation, and on the other, the local need for the services which the taxes procure. If, then, the older system of assessing and levying taxes and of expending them was justified on the ground of dealing with an actual situation in a practical manner, have we not good reason for asking that a totally new situation in these respects should also be dealt with in a practical manner? It is no criticism of either the justice or adequacy of the older system, when applied to the same conditions out of which it arose, to say that it is neither just nor adequate when applied to a totally new state of affairs which, without displacing the older conditions, has been super-added to them. The objection, therefore, to new departures in taxation which result from the changing shapes and conditions of property and the diffusion of its ownership is not complimentary to those who devised the older forms of taxation to which the objectors commonly adhere; for all that is asked is that we should deal with the new conditions in the same spirit as they dealt with the older ones; in other words, in a practical manner in the light of existing needs.

What, then, are the primary facts with reference to public service corporations, from the point of view of their possible taxation? Practically all of these corporations have to do with transportation or transmission. Financial corporations, such as banks, trust companies and insurance companies, are dealt with elsewhere in this program. Taking the most typical and important of the transportation services, the great railway companies, what are their characteristics? In a normal example we have a corporation the members of which — the stockholders — are, or may be, a changing body of individuals or other corporations. But even these members do not contribute all or even a majority of the capital which the corporation has invested; for modern railroads are financed chiefly by means of borrowed capital, for which the property of the corporation, either as a whole, or, more commonly, in specific sections of it, is formally pledged by mortgage. The holders of these mortgage bonds, like the holders of the shares, are or may be a changing body of individuals or other corporations, such as banks and insurance companies. Under modern systems of finance the capital which is contributed to a railway

or similar public service corporation differs, as between bonds and stocks, chiefly in point of security. Though the bondholders have no voice in the management of the corporation, yet, in actual practice, the majority of the ordinary stockholders have just as little voice in policy or administration. From the point of view of taxation bonds and stocks must be taken together as representing capital invested in the corporate enterprise. That range of territory, however wide it may be, representing at once the region of investment and of revenue, must be the region of taxation and not the place of residence of the holder of the securities. Moreover, the taxes should be levied upon the corporations and not upon the individual security holders.

In what form, then, does the property of such a corporation exist? Taking its chief terms, it is represented by long strips of land, expanded here and there for the location of switches, station yards, city terminals, etc. On this land is constructed the roadbed with its cuttings, embankments, viaducts, bridges and tunnels, and these carry the track with its ties, rails, switching and signal systems, etc. There are also the station buildings, freight sheds, elevators, machine shops, round houses, coaling stations and the costly city terminals and offices. Then there is the vast amount of rolling stock of all kinds and its equipment. To maintain and operate this great array of property there is employed an army of men, from general managers to porters, involving a heavy payroll. I leave out of account all the secondary enterprises in which a railroad company may be involved, in the way of hotels, parks, mines, timber limits, mills, lands, etc., as being not strictly essential to the functions of a railway as a public service corporation.

Here, then, is a vast organization extending over scores of taxing units, state and municipal, and serving many more which it may not actually enter, but from which it nevertheless derives revenue. The extent of territory covered and the capital expenditure involved in any given taxing unit has frequently little or no relation to the amount of service rendered within that area, the amount of revenue derived from it or the benefit obtained by the corporation from the expenditure of the taxes. Consider, for instance, the equity of taxing a

railway corporation, within a given township, on the basis of a very costly bridge and several costly cuttings and embankments which may happen to be located within it, while an immediately adjoining township, through which the railway did not happen to pass, could not share in the taxation, though perhaps contributing a much greater amount of traffic and hence of earnings, out of which taxes must be paid. Obviously, such a corporation stands related to the whole problem of local revenue and expenditure, state or municipal, on a totally different basis from that of private property and its resident owners. But we may leave aside for the present the question as to the proper jurisdiction under which the taxation of these corporations should come, and the proper system for the distribution of the taxes levied upon them. A primary question for consideration is the principle or principles upon which the value of a public service corporation may be determined for purposes of taxation.

Can we apply to the property of public service corporations the principles which are commonly employed in the assessment of private and business properties? In the case of ordinary property the two most pertinent questions are, what did it cost and what will it sell for? In every case, however, the question, what will it sell for? is of much greater practical importance than the question, what did it cost? In other words, the market value, where it is ascertainable, is the value which ultimately determines what anything is worth. But, unfortunately, we cannot apply this test of value or worth to public service corporations. There is no market for railroads, telegraph, telephone or express systems. It is true that they do occasionally change their managements, and, where their shares are actively dealt in, they are constantly varying in ownership. But these changes do not occur on the basis of the market value of each system as a whole. The change in management or control is effected either through a partial financial breakdown and the consequent appointment of a receiver, or through a change in the control of the majority of the voting power of the stock, either by a coalition of interests, aided, if necessary, by the purchase of a certain number of shares, or by any of the varied forms of agreement which have

been devised to secure control without the necessity for purchasing stock. But even where control is secured through the purchase of stock, the actual outlay represents but a small portion of the capital value of the system as a whole, inasmuch as it takes no account of the capital represented by bonds. It is evident then that there is no opportunity for determining the real worth or assessable value of public service corporations by the usual standards of market value for complete systems. Still less is it possible to determine in this way the value of any arbitrary sections of such systems which happen to lie within the area of this or that taxing unit, be it state, province or minor municipality. The portion of a railway or telegraph system which passes through a given municipality, or even a State or province, almost invariably derives a large proportion of its value, and sometimes almost the whole of it, from its connections beyond that area, or from its being but a link in a system whose chief revenue is derived from through traffic or transmission.

Neither is cost of production a fair test of value. Market value is the test which determines whether, in view of its cost, production should or should not be undertaken. It is, indeed, seldom proposed as a basis of valuation for public service corporations other than railways, and in their case it is proposed only because of the large proportion of tangible property required in their construction and operation. But even the most faithful advocates of cost of production, as a basis for assessment, admit that it may exceed or fall short of the full value of a system as a whole. How then is this variation from cost of production to be determined? The usual answer is, as given in Michigan, by ascertaining the general earning power of the system, from which is deduced the net earnings, which are then capitalized at some selected percentage, and this, it is claimed, will give the true capital value of the system. If now we deduct the cost of production from this true value, where it exceeds cost of production, we shall find what amount must be *added to* the cost of production in order to give the true value, which, however, was just the point from which we started. By a complementary process, where cost of production exceeds true value, we shall discover what must be de-

ducted from cost of production in order to get back to true value once more. But why we should undertake the enormous outlay in time and money necessary to arrive at cost of production, when, after all, it is capitalized earning power which gives us the true value, is by no means obvious on the surface of the proposition at least. When we penetrate below the surface, the explanation is commonly found either in the desire to force the facts to conform to some preconceived theory, or in the necessity, fancied or real, of conforming to some popular prejudice, embodied it may be in a state constitution, such as that all corporate property shall be valued and taxed on the same basis as ordinary private property.

But, it may be said, while it is true that public service corporations have no market value as complete systems, yet the securities which make up their total capital have market values, and by adding these together may we not arrive at their total values as corporations? To a certain extent the values of these securities represent the capitalized income of the corporations, and they are therefore a much more accurate representation of what a corporation is really worth than any attempts to estimate physical property or franchise values. But earning power is by no means the only consideration affecting the values of stocks and bonds, and particularly the former. The values of stocks, whether representing *bona fide* investment, promoters' interests, or merely an aqueous bonus distributed to bondholders or others, may be manipulated for purely speculative purposes over a considerable period of time, until unloaded upon an eager but unwary public. Certain issues of bonds, on the other hand, and even some of the best preference stocks are so completely held by private investors, or by various corporations, such as insurance companies, that for years they may never appear upon the market. Even where stray lots are sold, from time to time, they cannot be said to establish any regular market values for these securities. Again, the adoption, in varying degrees, of the policy of employing earnings for capital expenditure will correspondingly affect dividends over long periods, and consequently the value of the stocks. There is, further, a very common difficulty connected with the attempt to tax bonds in particular. While there is no doubt

that they represent a large proportion of the capital of public service corporations among others, still in point of law they represent no special interest in the corporations, but are simply securities for money loaned on the pledge of the corporate property. Hence, where they are held by foreign investors they are usually not liable to taxation. We must conclude then that the attempt to value corporations as a whole through a summation of their stock and bond values will produce very uncertain results, and with much inequality as between corporations.

It would appear to be more reasonable, therefore, to employ earning power openly and directly as the basis for corporate taxation. While private property is held for quite a variety of reasons, in addition to financial profit, practically the sole reason for the existence of economic corporations is pecuniary gain. Therefore, their value to their owners and operators, apart from speculative manipulation and trading in stocks, is represented by their earning power. Hence, it may be laid down as a broad principle that the earning power of a corporation represents its true value. Can that earning power or income be directly determined? In the case of private individuals, personal income is admittedly one of the most difficult facts to discover. With the ever increasing range and variety of investments and sources of income, it is increasingly difficult to ascertain, without the most inquisitorial methods, what may be the private income of most citizens. But, in virtue of the very nature of economic corporations, and of the character of the rights and obligations vested in the shareholders and officers, it is necessary that all the business transactions, including the income and expenditure, should be matters of definite record. It is impossible for a corporation of any magnitude or standing to dispense with an accurate system of bookkeeping which will record its entire income and outlay. There may, indeed, be much variety in the classification or definition of the items of income and expenditure, which will lead to obscurity and variation in the distinctions between gross and net income or between operating expenses and capital expenditure, but there is no difficulty in arriving at what is gross income and gross expenditure. It is true that

certain sums, amounting, it may be, to considerable items in the aggregate, may come temporarily into the possession of these corporations and be paid out again without representing either income or expenditure. Thus one public service corporation may act merely as agent for another, as in accepting moneys for services to be rendered by one or more companies beyond its own. But these sums can be easily ascertained as they are all matters of record in the books of the corporations.

Where net income can be ascertained it is in many respects the best basis for taxation. Net income, however, is very difficult to determine from year to year with sufficient accuracy for purposes of taxation. Endless discussion and dispute is certain to arise, and many opportunities for evasion are presented in connection with attempts to define what may or may not be legitimately deducted from gross income in order to arrive at true net income. No doubt if a uniform system of accounting can be established for public service corporations, toward the accomplishment of which the statistical department of the Interstate Commerce Commission is making laudable efforts, a fair approximation to net income would be possible. Although it is demonstrably absurd to insist that corporations must necessarily be taxed on the same basis as private individuals, it is not unreasonable to maintain that corporations should contribute their equitable share to the public revenue. If, therefore, the private individual does not escape taxation on property on which he may derive no net revenue, neither can the corporation which has no net revenue escape taxation any more than it can avoid paying customs duties on its imports. And what applies where there is no net income will apply with much the same force where there is very little net income. Even, therefore, if we could determine with perfect accuracy what the net revenue of a corporation was it might not be an admissible basis for taxation, or perhaps, more accurately, for the escaping of taxation.

It has been proposed as a sort of compromise between net and gross income, as a basis of taxation, that public service corporations should be taxed on the basis of the combined dividends paid on stock and interest paid on bonds, it being assumed that these returns represent between them what is

practically the net income of a corporation. It may be observed, however, that if no dividends are paid the interest on bonds may not represent any corporate income, but, to a certain extent at least, an element of capital expenditure, undertaken, it may be, for a number of years, to prevent the corporation from passing out of the hands of the stockholders, who may have faith in its ultimate success. If, on the other hand, it does pay a moderate dividend, this, in addition to the interest on the bonds, may not represent its full net income, as a larger or smaller portion of it may be diverted to other purposes, such, for instance, as an investment in the property as a whole, or in some collateral or subsidiary enterprise, having tax relationships quite different, it may be, from those of the parent corporation. Here the argument has been advanced that income which escapes taxation by being reinvested instead of being paid in dividends, by increasing the value of the property will, in turn, lead to increased dividends, and thus eventually replace the taxes evaded. This view of the matter, however, overlooks several important facts. In the first place, the taxes on the capitalized income are undoubtedly lost for a more or less lengthened period. When they reappear they are not taxed in the aggregate, as they should have been, but only on the extra dividends which may arise from them. Thus, suppose the net profits which are recapitalized should amount in five years to \$1,000,000, and suppose the tax rate which was escaped to be 2½ per cent, then the taxes lost in the five years would amount to at least \$25,000. Suppose the subsequent dividends paid on this new investment of \$1,000,000 to be 6 per cent, then the dividend on the proportion of the taxes escaped will be \$1500, and the taxes on that at 2½ per cent will be \$37.50 annually. But this will obviously require a very long period to make up for the original evasion of \$25,000 in taxes.

There are many other difficulties attending this among other attempts to determine and tax net earnings so as to provide a fair annual revenue. The alternative is, of course, to take gross earnings as a basis for taxation. This method of taxation, it is true, is not without its own defects, but they are much fewer and much less serious than those attending any other system. There is, as we have seen, little or no dispute as to

what are gross earnings, and as taxation has as legitimate a claim against the gross earnings of a corporation as any item of operating expenses, it is not unjust to deduct the taxes from gross earnings, even where no net earnings remain. No doubt, as between corporations which are prosperous and those which are not, the taxes will be felt with unequal pressure, but so will every other necessary item of operating expenses. But while it is legitimate to tax the gross earnings of corporations having little or no net earnings, it is desirable to have a graded rate, so that the taxation may bear more lightly on those having little or no net income, and more heavily upon the more prosperous corporations. In fixing the rate of taxation on gross earnings according to ability to pay, the net income of corporations, so far as it is ascertainable, may be employed as a guide. In practice, however, it is found that the great majority of normal public service corporations will fall within one, or at most two classes, leaving only exceptional cases as requiring separate treatment.

Once it is admitted that the earning power of a corporation is its true basis of value the chief question which remains is as to the rate at which the income, whether net or gross, is to be taxed. In the case of railway companies, net income is normally about one third of gross income. So that approximately a tax of 1 per cent on gross earnings would be equivalent to a tax of 3 per cent on net earnings. When, however, we attempt to compare a tax on the income of public service corporations with the various taxes paid on private property, we are immediately confronted with the difficulty of finding any satisfactory basis for comparison. The only fair basis of comparison would be to take the gross or net earnings of both corporations and individuals. But here we are met with the fact that, while we can ascertain with reasonable accuracy the gross earnings of a corporation, it is almost impossible to discover the gross income of the ordinary business man. If we turn to specific forms of property and compare a tax of, say, 3 per cent on the gross earnings of railways, with the common tax on the gross earnings from real estate, we should probably find that the railways were paying too little. But if we took the taxes paid on most other kinds of property as a basis for comparison,

we should probably find that the railways were paying too much. It is impossible here to go into details on these matters, but a careful study of the subject will prove, I think, that no very satisfactory practical conclusion can be reached in attempting to fix an equitable rate of taxation for railways through comparison with the taxation of ordinary private property or the income derived from it. As public service corporations must be valued on a special basis, so their rate of taxation must be fixed upon a special basis. The attempt, in the interest of a superficial and mechanical equality, to value, rate and tax public service corporations on the same basis as the property of private individuals cannot fail to result in very real inequality in taxation.

One very important reason for the special treatment of public service corporations, as regards taxation, lies in the fact that, under modern conditions, the public is ever more insistent on regulating the rates and charges of these corporations, and otherwise closely supervising their services and their obligations to the community. These public regulations naturally restrict within very definite limits the opportunities of the corporations to augment income, or even to maintain it. If, therefore, the public insist upon having cheap rates, they must, in all fairness, correspondingly moderate the taxation of the corporations; for regulating rates is levying taxes in kind.

After a careful survey of the various aspects of the subject and a comparison of views with representatives of taxgatherers and taxpayers, I have been led to believe that a tax of 3 per cent on gross income is a sufficiently high tax for railways, with not more than 2 per cent for other corporations. Lower rates, however, should be provided for exceptional cases where there were obviously few or no net profits; but, as already indicated, the absence of net income is no valid argument against a certain minimum of taxation.

Some difficulty has been met with, on technical constitutional grounds, as regards the taxation of public service corporations whose operations extend, as most of them do, beyond the limits of state or provincial taxing areas. It is even yet apparently somewhat of a moot question as to whether it is constitutionally admissible for a State to tax a corporation upon its earnings,

where these are derived from interstate services. But where this position is taken with reference to earnings, it is commonly held to be quite constitutional to tax interstate corporations upon the basis of their property or their franchises, as within the State. Yet it is perfectly well known that the value of the property or the franchise within the State is really determined by the relation of these to the whole system. Moreover, the value of the property as a whole is chiefly dependent upon the extent of the interstate traffic. Taxes also, on whatever basis levied, are obviously paid out of interstate earnings. The distinction therefore between a property tax as constitutional and a tax on earnings as unconstitutional is a legal fiction of a very inartistic character. But like so many other difficulties arising from historic conditions it arises from the fact that a service which was at one time purely local has enormously expanded in importance and range, and has become the function of interstate corporations many of which are now of quite national character. This expansion of several interests from local to national importance is leading many of those who fully respect state or provincial rights, to recognize that a service which has passed beyond the range of state or provincial territory and become national in its character, should, if necessary, be dealt with by national laws. The normal line of escape from the absurdities born of constitutional interpretations based on more elementary conditions which are rapidly passing away, would be for the various States or provinces to arrange periodic conferences to determine the fair amount of the earning power of each system as a whole which should be assigned to the individual States or provinces. Should they find it impossible to agree upon such an apportionment, they might either call upon or permit the federal or national government to assess — not to tax — the earnings of public service corporations, distributing the values among the different States or provinces upon an equitable basis. Either method would avoid the increasing confusion, injustice and inequality which result from leaving the taxation of interstate public service corporations to the caprice of individual States. By purely arbitrary systems of valuation, individual States and provinces have been able to levy more than their just share of taxation upon the corpora-

tions whose lines of transportation or transmission pass through their territory.

In distributing within each State the assessment apportioned to it by mutual agreement among the States or by the national government, the municipalities might still be allowed to assess the value of the lands and buildings owned by a public service corporation within their limits on the same basis as adjoining lands and buildings. After these taxes were deducted from the gross amount allowed to each State, the remainder could be applied to state or municipal purposes, as determined by the legislature of each State.

It is unnecessary in connection with this brief statement to specify all the advantages, practical and scientific, which would result from a uniform assessment and distribution of the taxation of public service corporations upon the basis of their earnings. It is, however, obvious that every step in the expansion of the economic interests of the United States and of Canada involves the increasing importance, alike from a local and from a national point of view, of the services of transportation and transmission and the corporations which supply them. This expansion involves the investment of new volumes of national wealth with increasing aggregate returns in the way of income, and, consequently, of tax-paying power. But as these forms of wealth cannot be dealt with adequately or justly by the older methods of local taxation, it is imperative that some movement should be made toward devising a method of assessment and distribution on a wider basis and in accordance with their true economic value. Only in this way can we meet actual conditions in a practical manner.

TAXATION OF PUBLIC SERVICE CORPORATIONS

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THERE is a marked tendency in the United States to apply to corporations methods of taxation different from those applied to individuals. This tendency is most pronounced in those States whose economic development is most advanced. It arises mainly from the inadequacy of our old taxes to reach the tax-paying capacity of the large corporation. But it seems also to be closely related to certain recent developments in the social and economic philosophy of the times, especially to those philosophical tenets which concern the social control of the larger industrial enterprises. Government regulation of rates, the opposition to monopolistic combinations, the prohibition of discrimination, the popular condemnation of stock watering and similar abuses or manipulations of corporation capital, the demand for publicity of accounts, are all the outcome of a trend of thought which has a deal to do with shaping our tax laws.

This essay is, however, not concerned with these larger questions of social control, but will be an attempt, as if made on the part of a fiscal officer, to answer the practical question, "How can the government most easily and surely obtain from those larger industrial enterprises now for the most part conducted by corporations a fair contribution in the way of taxes?"

The legal and economic right of government to apply to corporations a method of taxation different from that applied to natural persons rests on the obvious fact that the corporation is a special creation of government, and the natural persons associating together to form the artificial person enjoy therefrom certain advantages not enjoyed by those not so specially privileged. It is clearly within the powers of the government

when it creates or continues these special privileges to place upon them such limitations as it sees fit. It may consequently tax them as it sees fit. Ordinarily no fiscal officer would assume that this power to tax the special privileges enjoyed by corporation could be exercised to such an extent as to destroy the privileges. But it is certainly within the discretion of the legislative authority to exercise the power of taxation even to that extent.

The movement toward special forms of taxation for corporations in the United States is comparatively recent. If we except Pennsylvania and Massachusetts, which were the earliest to establish a clear differentiation between the taxation of corporations and that of individuals, and New York, which has been some twenty-five years evolving such a system, and if we regard the "specific" taxes of Michigan and her neighbors as sporadic or accidental exceptions, we may assert that the whole movement has taken place within the last twelve years. While it is still true that the great majority of our States to-day depend primarily on the general property tax for the taxation of corporations and individuals alike, yet of the fifty-one States and territories in the Union, fourteen, namely, Connecticut, Delaware, District of Columbia, Maine, Maryland, Massachusetts, Michigan, Minnesota, New Jersey, New York, Pennsylvania, Virginia, West Virginia and Wisconsin, have already adopted radically distinct methods for taxing corporations; of the remainder the great majority have at least started along the road already traveled by the fourteen leaders; only six, namely, Alabama, Colorado, Louisiana, Mississippi, Montana and Nebraska, can be said not to have passed the first mile-post, and of these six, two are now actively inquiring the way. In short, there are but four commonwealths which have not felt the sway of the new ideas.

An analysis of the methods of taxation applied to corporations in the more advanced States shows a more or less general recognition of four different kinds of special privileges as the bases of special taxes or special methods of taxation. The first of these is the *right to become a corporation*. This is everywhere subject to fees payable at the time of incorporation which vary in amount from the mere compensation for official labor in

issuing papers to a sum which constitutes of itself a good stiff tax. The second of these is the *right to continue to be a corporation*. This is, in many of our States, now subject to the payment of an annual fee or license. This tax is among the more recent additions to our list of corporation taxes. It serves, besides its undoubted revenue-yielding function, to secure a current record of active corporations and to eliminate dead companies from the rolls. As the rates are usually graduated according to capital, it also tends to prevent over-capitalization. The third special privilege is the *right to do business in a way not granted to private individuals, or to do some particular business not ordinarily permitted to private individuals*. The States of the old South through their highly elaborated system of license taxes have developed the taxation of this special privilege more distinctly and in a more easily recognizable form than has yet been possible in the Northern States. But for special groups, like banks and insurance companies, this is a very common subject of special taxation. In some cases the taxation of this privilege has been so far extended as to cover elements akin to good will which are not taxed ordinarily when enjoyed by private individuals.

The fourth or last group of special privileges enjoyed by corporations which have been made the subject of special methods of taxation are the special franchises enjoyed almost exclusively by "public service corporations." These are privileges the enjoyment of which is never conferred except explicitly, and are distinctly in addition to the ordinary corporate privileges. In most cases they involve a partial delegation of government powers. They almost invariably result in monopoly or form the basis for monopoly, and are often extremely valuable. It is furthermore usually true of them that they have grown in value as time passed far more rapidly than was anticipated when they were granted.

There have been four different ways used in the United States for reaching this fourth class of special privileges for purposes of taxation. These are: (1) the property tax; (2) the net earnings tax; (3) the gross earnings tax; (4) the license tax. The oldest and still the most prevalent is *to treat these privileges as property* and include them in the valuation of the

taxable property. The valuation may be arrived at in two ways: (1) by valuing the tangible property and then adding an amount equal to the difference between that and the value of the stock (including bonds). This difference is called the "corporate excess" in Illinois and other States, the "value of the franchise" in California and others, or more generally the "value of the intangible property"; or (2) by ascertaining the earnings and capitalizing them, thus obtaining the value of the aggregate properties, and then proceeding as before by deducting from this aggregate the appraised value of the tangible property, thus obtaining the value of the corporate excess "of the intangible property."

The taxation of these special privileges as property is a plan which has many able advocates. The fact that two States, Michigan and Wisconsin, which had another system originally, adopted this plan after prolonged discussion and agitation has given it considerable recent prestige. But it is open to several very pronounced and serious objections. In the first place this system requires that the board, commission or officer making the valuation shall be vested with discretionary powers which cannot be characterized as other than arbitrary. These powers must be so large that if not exercised with due reserve, they may be destructive. Vesting any elective or even appointive officers with such power in regard to public service corporations has the practical effect of dragging those corporations into politics for the purpose of controlling such officers. Even if the price of reduced taxes, often amounting to many hundreds of thousands of dollars per annum, be not lure enough to tempt the corporations to struggle for the control of these boards, there is still the prod of necessity to prevent the election or appointment of a hostile board or official. Experience has shown that while it is possible for a few years, as in Michigan and Wisconsin, to establish reasonably public spirited boards of assessment, yet that after a time these boards usually become, if not subservient to the corporate interests, so inert as to be ineffective for the protection of public interests.

Directly connected with this danger is the tendency, inevitable if judged by all historical instances, for the assessment, when made on an *ad valorem* property basis, to crystallize and become

rigid. One has only to compare the growth of the assessment of railroads (the most easily available data) in those States which have used this system for any length of time with the growth in the valuations placed on other property, or, for a more telling contrast, with the growth of the gross and net income of the same railroads, to be convinced of the strength of this tendency. Any board, whether subservient to the corporations or not, after it has once made the extensive investigations necessary to fix a valuation, say, on railroad franchises, is most naturally prone to regard that as final and conclusive for some years to come. It may make additions to the assessment for improvements and for new property acquired, but it is not apt to revise its valuation of the original property. Only when such a board is sturdily enforcing some other system of taxation, under the guise of a property tax, does this tendency remain in abeyance.

That so many States still rely on the property tax for this purpose is explained: first, by the fatuous confidence of the American people in the all sufficiency of that tax in all possible contingencies (a confidence ill sustained by experience); second, by a certain confusion of thought, namely, that "equal taxation" can be attained only by applying the same form of taxation to all subjects, irrespective of differences in their character; and thirdly and lastly, by a misunderstanding of the exact scope of those constitutional provisions which safeguard interstate commerce. Of the first of these stumbling blocks it is sufficient to say that the present leaders of American political thought are unanimous in their view that the property tax is inadequate to reach all the forms of tax-paying ability which modern civilization presents. The notorious failure of this tax to reach personal property, for example, has become a favorite subject even for schoolboy debates the country over. On the second point one has only to attempt to fathom the meaning of the popular slogans used in any one of the recent tax-reform movements to be satisfied that in the popular mind "equal taxation" means merely "taxation by the same method"; as though one could justly tax a printing press, which runs 365 days of 24 hours each per annum, on the same basis, namely, that of cost of construction, as a hay press, which runs only 30 days of 12 hours each per annum.

Shallow as are in point of fact the first two of the above-named current objections to any departure from the general property tax as applied to public service corporations, the third is merely fallacious, and rests upon ignorance of the principles which guide the Supreme Court. Unless there is a deliberate attempt to limit by means of taxation the free interchange of products between the several States, the Supreme Court of the United States has never once interfered with the States as to the choice of the *form* of taxation for corporations engaged in interstate traffic. But on account of the awe in which our Constitution is held, ignorance on this point is very potent. A few years ago Canada sent a commission to this country to investigate the methods in vogue for the taxation of railroads. That commission rendered a report which for ability and obvious evidence of diligence is not easily surpassed among public documents dealing with taxation. The clear vision of these commissioners showed them the fallacy of the first two points above referred to, but so current, even among recognized authorities and among our leading attorneys with whom the Canadians conferred, was the third error that this sagacious commission carried away the impression that any method of taxation other than the property tax was unconstitutional in the United States as applied to corporations doing an interstate business. Yet in the face of this current legal view Justice Holmes, in voicing a unanimous decision of the Supreme Court of the United States, a decision in which all the wisdom of that court on this point for a century is reviewed and summarized, brushes aside a long argument with the curt statement, "We need say but a word in answer to the suggestion (he does not dignify it as an 'objection') that this tax (a tax based on gross earnings) is an unconstitutional interference with interstate commerce." The same court had previously said in regard to a tax on the property and franchises of a corporation engaged in interstate commerce, the tax being based solely on gross earnings, "that a tax of this character is within the power of the State to levy, there can be no question." (*Maine vs. Grand Trunk Ry. Co.*, 142 U. S. 217.)

If we reject the property tax on the ground of its inadequacy when applied to public service corporations, we are

apparently confined to a choice between net earnings and gross earnings as a basis for taxation. Taxation according to net earnings has some very able advocates, who have built in its defense a very strong argument. If we turn away from property as a basis, it seems natural to turn first to net earnings as that which gives the property its value. When, however, any fiscal officer tries to devise a net earnings tax which will work with some degree of justice and still yield the necessary revenue, he finds himself confronted with difficulties even greater than when he tries to make a property tax effective. By long experience our law makers and our officials have acquired a somewhat definite idea of what constitutes property and of how to ascertain its value. But experience offers no such clew to what is by nature a "net" item in, say, a railroad account. The placing of any item as "net" is largely a matter of bookkeeping, and may be changed in a day by a vote of the directors or even by the instructions of an auditing officer. If taxes are to be based on net earnings, the government must not only supervise the bookkeeping, but prescribe its forms and methods, and for adequate protection it would have to dictate the character, if not the amount, of all expenses that could be deducted. That means that the cost of enforcing and collecting a net earnings tax would be well-nigh prohibitive. Furthermore, the rates would have to be so high that the temptation to enter politics for the sake of modifying those rates or the definition of "net" earnings would be greater than the public service corporations could be expected to resist. An arithmetical example will make this clear. Our railroads count, on the average, about 36 per cent of their total earnings as net. Assume for the moment that 1 per cent on the full cash value of the property is a fair tax and that 6 per cent is the rate at which we would capitalize earnings in determining the value of the property. Then for every \$100 of gross earnings we should have \$600 of capital and the fair tax would be \$6. This is 16 $\frac{2}{3}$ per cent of the net earnings, a tax rate so high as to put an enormous premium on manipulation of accounts, and to hold out a glittering reward for the political control of the taxing authorities. It would seem then that the practical difficulties in the way of administering

a net earnings tax, namely, expense, uncertainty, danger of political interference, and probable evasion and inequalities, are prohibitive.

A gross earnings tax at a fixed rate for each of the different classes of public service corporations seems, therefore, the only recourse. The objection to this may be stated first: such a tax may not be absolutely equitable between the different companies within a class when measured either by property value or by net earnings. There may be a railroad, for example, whose net earnings are far above the 36 per cent average, which would apparently gain by such a tax, or, *vice versa*, one whose proportion of net earnings is low, which might, perchance, suffer. Forceful as this objection may seem when first stated, it has been found to have comparatively little weight when investigated practically. The Canadian Commission, to which reference has already been made, ascertained by a careful study of every road in Ontario that none would be really injured and none materially advantaged road against road by such a tax. The recent California Commission, after investigating in a most thorough fashion every railroad in that State which might be affected, including roads operated under conditions almost as varied as imagination can suggest, found that such a tax would be very nearly equitable for every road, with the possible exception of one. That one was a small narrow-gauge road operated in connection with a steamship and lumber company in such a way that the accounts of the three departments were so inextricably intertangled that the net earnings were not easily distinguishable so that the fact that it was an exception was a matter of grave doubt.

The economic explanation of this apparent anomaly is probably to be found in the actual outworking of the long-recognized principle that "the rate of profit on capital in all employments tends to an equality." (Mill, "Principles of Political Economy," Book II, Chapter XV, Section 4.) It is important in this connection to recall to mind that public service corporations are industrial or capitalistic *monopolies*, and that as monopolies they cannot shift a uniform gross earnings tax. Furthermore, no proportional gross earnings tax can change in any way the point of highest net returns, as it simply de-

presses the whole curve of rates by a uniform amount. In short, it is mathematically impossible for a uniform gross earnings tax to work great injustice between subjects of the same class, except in those exceptional and incompletely developed cases in which the expenses are increasing by irregular leaps as the business grows. Stated in less technical terms, the value of the public service enterprise depends on the amount of gross earnings which the manager has to conjure with, and a tax in proportion to those gross earnings can but little, if at all, disturb the relative advantages which the various companies may enjoy. The objection to gross earnings tax seems therefore to be weak.

On the other hand, the advantages of the gross earnings tax are many and obvious. The base is an easily ascertainable fact. It is not subject to bookkeeping deductions, nor can it be manipulated or falsely reported save by perjury of the most pronounced and easily detectable character. This tax requires no supervision of corporation bookkeeping, and no interference with the internal management of the corporation. The determination of the amount to be paid is a mere arithmetical computation which any newspaper, any citizen, can check up. It does not call for the vesting of administrative commissions or officers with wide discretionary powers. The tax is always in direct proportion to the fund out of which it must be paid. In short, it is safe, certain, non-evadible, inexpensive in operation, adequate, if the rate be high enough, and as equitable as, if not more equitable than, any other tax applicable to public service corporations. It will yield a revenue which will grow as the needs of government grow. It reaches, effectively, the "unearned increment" which public service corporations enjoy, without confiscating that part thereof which the original adventurers in the enterprise are entitled to under our dominant conception of the rights of private property. It fulfills the demands of a fiscal officer who wants a tax as effective, from a revenue-yielding capacity, as possible and at the same time fairly equitable. In passing it may be noted that lack of efficiency is sure to result in inequity.

It is sometimes urged as an objection that the yield of such

a tax fluctuates without reference to the needs of the government. An extensive study of this feature shows that as a matter of fact it would not fluctuate any more violently than to have the property taxes actually levied on the same classes of corporations, and that as compared with such taxes it grows far more rapidly in revenue-yielding power. It may further be urged that as any decline in the earnings of public service corporations is coincident with "hard times," it would not be unbecoming for the government then to retrench its expenses as private individuals are forced to do.

The fourth method of taxing public service corporations, namely, by special annual license taxes, has been so little developed that we have but little experience to guide us in judging its efficiency. It is used in connection with other taxes in some Southern States as a part of a general system of business licenses. The yield is never adequate, and while it may reasonably be used to fill in the lacunæ of some other tax or taxes, it cannot be easily adjusted as a sole tax. It is doubtful whether in the Northern States, which have in general surrendered the field of license taxation to the local governments, any revival of this system would be desirable.

The gross earnings tax seems to be adapted to the taxation of the following classes of public service corporations: first, all those engaged in transportation, of which we have at present the railroads, including street railroads, the car companies and the express companies; second, those engaged in furthering communication, the telegraph and telephone companies; and third, those engaged in the production, transmission and sale of light, heat and power. Incidentally it is peculiarly well suited to the taxation of insurance companies, but as these are hardly to be classed as public service corporations they fall without the scope of this essay. It is ill adapted to the taxation of water companies. This fact becomes apparent the moment one tries to determine a fair rate for a group of actual water companies. The economic reason for this is probably to be found in the fact that water companies enjoy "natural" rather than "capitalistic" monopolies. Their profits depend upon local advantages or disadvantages, and are not governed by those leveling tendencies which affect

all these industries into which capital can more readily flow when exceptional profits are revealed. The water company, whether engaged in irrigation or in domestic water supply, is closely connected with the land. The value of its plant is determined by and contributes to local land values in such an intimate way that the values of the two are both controlled by the same laws. This points to the same method of taxation for each, that is, for land and for water companies, and certainly the gross earnings tax is not applicable to land. As in the case of landowners, so in the case of water companies, the potential resources are often but partially utilized, and a gross earnings tax would not reach these unused resources as a property tax would. Moreover, the case of water companies is complicated by the numerous publicly owned plants. So far as experience is yet available, it is doubtful whether anything better than the property tax can be devised for water companies. It may as well be, however, that cities and municipal districts under irrigation would be wise to collect a fixed percentage of the gross earnings of water companies in addition to the property tax, this percentage being regarded not as a tax, but as part payment for the sale of public rights.

The determination of the rate of taxation which should be applied to the gross earnings of different classes of corporations is not so difficult as might at first thought appear. We have a fairly accurate idea of what constitutes a just tax on property. In the United States at large the average for real estate, the only class of property fully taxed, is not far from 1 per cent on the full market value of the property. For purpose of illustration we may assume that 1 per cent on property is a fair rate with which to compare taxes levied on some other basis. Should some one else decide for his own part that some other rate is fair, he can easily raise or lower the rates at which we may arrive in proportion as his "fair rate property" is higher or lower than 1 per cent. For purpose of illustration, further, our assumed 1 per cent renders the computations much simpler and the examples clearer. In each of the different classes of public service corporations there is a distinct trend towards a uniform ratio of net to gross earnings. Capital, in seeking investment, demands an average

return. If investments in any one line of public service corporations, say, telephones, yield an unusually large return, more capital enters that line, until its profits are equalized with those in other lines. So, too, if any one line yields less than the normal profit, no new capital moves in that direction until its earnings there rise to normal. The amount of capital which any enterprise can carry is determined by the net earnings. The proportion of capital to gross earnings is, therefore, what we need to know in order to determine what rate of tax on gross earnings is the equivalent of an assumed fair rate on property. This is, in turn, dependent on the ratio of net earnings to gross. It is pretty well established that the net earnings of railroads approximate on the average closely to 36 per cent of the gross, the same is true of street railroads, with a proper allowance for depreciation not often properly charged in the current accounts of such companies. In the case of express companies which require a far less proportionate amount of capital, the proportion of net to gross earnings is about 15 per cent on the average. The amount of property is relatively small, especially if one disregard intangible property. As the United States Supreme Court found in the famous Ohio Express Company cases, "\$23,400 worth of horses, wagons, safes and so on, produced \$275,446 in a single year." In the case of car companies, with proper allowance for depreciation, the proportion of net earnings to gross is closely approximate to that of railroads. For telephone companies the ratio is a little less than 20 per cent and for telegraph companies a little below 25 per cent. The case of light, heat and power companies presents greater difficulties on account of the rapid changes going on in the methods of production and transmission which make the rate of depreciation on the plant very rapid and very uncertain. With no allowance for depreciation they appear to earn 60 per cent net on the average, but with proper allowance for that element their net earnings appear to average something over 33½ per cent.

Under the system of separate sources of revenue for the State governments as distinct from the sources of revenue for local purposes, a plan which a considerable number of States have arrived at and toward which others are working, all these

public service corporations would naturally be taxed for state purposes only upon all but non-operative property. This is because they are general, not local, in character. Even the street railroads are an integral part of the general transportation system, and the light, heat and power companies which string their wires over hundreds of miles have nowadays no single mere local habitat.

The questions connected with state jurisdiction, the questions of interstate comity involved in the taxation of public service corporations, present a peculiar set of difficulties. These are, however, no greater under a gross earnings tax than under a property tax, in fact they are easier to answer under the former. It is easier to apportion the gross earnings fairly between States than to apportion the property. The property can be apportioned only on a mileage basis which gives those States with long miles of sparsely settled country through which the public service corporations operate an unfair advantage and robs those of denser population of revenue which is peculiarly their own. A gross earnings tax may be apportioned on a mileage basis as is the case with the tax on railroads in Maine, or it may be apportioned on the basis of business done as is the railroad tax of Minnesota. The latter is decidedly the more equitable between States. But if neighboring States, one densely populated and another sparsely populated, have antagonistic systems and the sparsely populated one were the one to adopt the straight mileage plan, it might work a hardship on the public service corporations. Sooner or later this must be a subject for federal regulation. The federal government must either collect all the taxes from public service corporations engaged in interstate business and apportion the proceeds among the States, or it must lay down set rules according to which alone the States may tax such corporations. Probably the latter is the more feasible plan. Meanwhile, we shall be obliged to content ourselves with such rules of interstate comity as our American sense of justice and fair play may develop. Such rules, if ever developed, will occupy, so far as concerns the States of the Union and their tax relations one to another, the same place as international law between nations. So far as public service corporations

engaged in interstate commerce are concerned the only equitable rule of "interstate law" would be, "Let each State tax all the business done entirely within its bounds, and such proportion of all interstate business as the mileage of such business in the State bears to the total mileage over which such business is done."

The writer of this essay respectfully recommends to the National Tax Association the proposal to the States of this rule as part of a code of "interstate law," and further, the indorsement of a tax on the property and franchises of public service corporations based on their gross earnings within each State as defined by the above rule, as the most equitable and expedient method for the taxation by the States of the various classes of general public service corporations.

SPECIAL FRANCHISE TAXATION IN NEW YORK

BY GEORGE S. COLEMAN

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WHAT is known as the Special Franchise Tax Law of New York was adopted in 1899 in pursuance of the persistent efforts of Governor Roosevelt. Upon the day before the assembly adjourned for the session, he sent an urgent message, requesting that body to follow in the steps of the senate, which had passed the bill. The assembly did not act upon that message, but the next day the Governor sent another message in which he said that while the bill presented might be defective in form, it ought to be passed, and that if necessary it would be amended. The assembly passed the bill. A month later the Governor called an extra session of the legislature to propose amendments which he thought vital. The three things he desired were, first, to make the tax one on *real estate* (to prevent deduction of debts); secondly, to have the valuation made by a state board and not by local assessors; and thirdly, to have express provision in the act for a deduction from the tax imposed of certain payments made to the locality where the property was situated, such as license fees and percentages on gross receipts from operation.

The legislature passed the act in the form submitted by the Governor, with a trifling change which under judicial decision made no difference in effect. It became Chapter 712 of the laws of 1899. It was not a separate and independent working statute; it merely amended four or five provisions of our general Tax Law. The new provision was that which taxed the *value of the right to operate*. We had always, or for many years, taxed railroad tracks, telegraph lines on poles, electric wires underground, etc., as real estate. The innovation in the law consisted in adding to the valuation of such property the value of the right to maintain, construct or operate those properties in, on, under or over the public streets or highways of the city.

The tangible and intangible were united in the "special franchises." The Governor was firm in the opinion that millions of dollars of value had escaped taxation, and that it was but fair to the small farmer or merchant that some of the burden of taxation should fall upon this property, which had never been, as he thought, adequately taxed in the State of New York.

As might be expected, this bill met with vigorous and persistent opposition. Various objections were urged against the validity of the act. It was attacked on the ground of violating "home rule," because, it was contended, under our Constitution, assessments of local property should be made by local officers elected or appointed under legislative authority. It was opposed under the federal Constitution, because it was said to impair the obligation of a contract; the idea being that when a locality had granted a franchise to a corporation, upon certain conditions, it was estopped from adding a further burden upon the right that it granted. It was further opposed because it was said to be impracticable. After a long legal battle the courts of New York sustained the validity of the act,¹ and the decision of the Court of Appeals was affirmed by the Supreme Court of the United States.²

Naturally, as soon as the law was pronounced valid, the next attack was upon the valuation placed on this new species of property, in the effort, apparently, to minimize the effect of the law by whittling away the value of the intangible right to operate. Proceedings have multiplied until there are hundreds of them now in the courts. Not in a single case, so far as I am aware, has a decision been reached that will enable us to say what is the prescribed method of valuation.

I have listened with great interest to the two papers which have preceded these remarks, to discover something that might be helpful to our courts; but as we do not tax on the gross earnings basis, or on the net earnings basis, we must somehow find the value of the property in the streets, together with the intangible right to operate it. The law itself prescribes no method.

Referring to what Professor Shortt said in criticism of the roundabout way of valuation, it seems to be absolutely neces-

¹ 174 N. Y. 417.

² 199 U. S. 1.

sary, in many cases, because where a public service corporation has property in the streets and property outside of the streets, and both contribute to the earnings, our law will not permit us to assess the value of the property off the streets as a part of the special franchise; we must eliminate that. It seems therefore to be necessary, first, to find the value of all the tangible property that contributes to the earning, from operation, and then, when we capitalize the net earnings, to deduct the value of the property off the street. It seems a very simple thing. But like some of the general propositions of the federal Constitution, the rule is simple only until you come to apply it. We have had three or four proceedings already involving the method of valuation that have been determined by referees, but none yet passed upon by the courts. In one case a part of a rapid transit system was assessed. This rapid transit system was operated by a company having a half-mile of track; it was owned practically by a corporation that did not operate a foot of track, but by combination of these roads and by ownership of controlling interest in the stock, the little half-mile company operated several hundred miles of track daily, and the proceeds of the operation of these companies went into one general coffer and were transferred by a system of bookkeeping to give equitably its proper share to every constituent company. It was impossible for even those who represented the corporation assessed to tell precisely what the earnings of any one company were, or what its operation cost. The referee treated each separate line as part of an entire system; and where one of these lines ran from Queens County into Kings, he credited the portion in Queens with its share of the net earnings of the entire system, and charged it with its share of the net expense on the car mileage basis, and on that basis found a value which he thought was just. That has not yet reached the courts for decision. This particular company had no power house; its power was supplied by the operating company; therefore, it could not be said to have property outside the street.

In another case it was a water company. The water company had pumps and driven wells off the streets and mains in the streets. The point there presented was, when it came to capitalising and allowing a fair return, should we allow a return

on the increased value of its real estate, or should we give a fair return on what that real estate cost, — because there had been an increment in the real estate since the formation of that company? The referee sustained the assessment as made, on the theory that capitalizing the earnings, on the basis he took, left nothing for reduction, even on the theory that it was entitled to be equalized with other property in the same district.

The last case in which there has been serious litigation, which has not yet been decided, was that of a company whose capitalization was ten millions — I mean its own estimate of the value of its plant used in operation. It had a bonded debt of about thirty-five millions. Its capital account showed that about twenty-six millions had been expended in order to create that plant. That was book value. They did not, of course, expect to get any credit for what they called "lost capital," but their claim was, that when we figured the expense of operation and deducted that from the income, and made certain other deductions for a *sinking fund*, then, capitalized on any sensible theory, the result would be, instead of having added something to the value of their tangible property, we would actually get a lower valuation than if the Franchise Tax Law had never been passed. That case is in the hands of the referee. Of course, it is idle to speculate as to what the courts will do in cases of that kind.

Some of the questions likely to arise in many of the proceedings now pending may be briefly noted. It is urged that under our system we must take the net earnings and capitalize them; but before we determine the net earnings, it is proposed to take out from the gross earnings, in addition to operating expenses and taxes, a certain sum of money each year as a sinking fund for depreciation, so that at the end of the first period, measured by the estimated life of the plant, the capital will remain intact, in the shape of a replacement fund. Assume the period to be twenty years. In a case in point it was proposed to set aside \$440,000 a year. If that were done for twenty years and the interest on that annual sum compounded, at the end of the twenty years, instead of having a fund of \$10,000,000 to replace the plant, you would have a fund of several millions in *excess and the plant besides*; because no railroad company can

allow its tracks to become dangerous; it must maintain its tracks and equipment in a state of efficiency, and at the end of twenty years, so far as the tracks are concerned, they will be as serviceable as they are to-day. If the given life is twenty years, estimated on an average, some of those rails will be taken up in ten or twelve years and replaced with new; almost everything will have been replaced, not all at the same time, but at the end of twenty years almost everything will have been replaced, and the cost charged to operating expenses and deducted from gross earnings. We think the claim for annual allowance was excessive. It may be proper in some cases to allow something, but whatever is laid aside beyond that which is required for replacement, whatever is laid aside and not distributed, is just as much a part of the return, as a result of operation, as that which is distributed in dividends. The question is not, where do those net returns go, but how much are those net returns? The net returns, over and above operating expenses, including maintenance, should furnish the measure of capitalization.

Another question is, how to treat *enhancement of value*? In New York City real estate is advancing so rapidly in value that you may afford to receive no immediate returns on its purchase price, for in the course of ten or fifteen years you may find the value doubled. Out of gross receipts allowance is made for taxes and insurance, expenses on property, repairs, etc., and if the company should receive no return for the land or building, except on the basis of *cost*, yet the lot itself would have greatly enhanced in value in ten or fifteen years. It is urged that the company is entitled to a return on its *present value*, and it is replied that it is entitled to a fair return only on what it cost.

A further question is, on what basis should we capitalize net earnings? If you have laid aside a fund against emergency, if you have taken care of all the operating expenses, if you have then a certain net return, shall you capitalize at 6 per cent — the rate of interest in our State — or at 5 or 7 or 4 per cent? In the hands of the shareholder that share is exempt from taxation. If he receives 4 or $4\frac{1}{2}$ per cent net return (under a perpetual franchise) on his original investment, with the possibility that by proper management the stock will

enhance in value, — a possibility not shared by the holder of bonds or mortgages, — has he received a fair return? Must he receive 6 per cent because that is the legal rate of interest? That is a question which may be discussed and argued for hours upon either side and has not yet been settled in our State. It is possible that different rates of capitalization may be adopted by the courts for different kinds of business, or even for different corporations engaged in the same business.

In the brief time allotted for consideration of the subject it is impossible to discuss the language of the Special Franchise Act or the few decisions that have been rendered on some of its provisions. The questions actually raised and still undetermined are full of interest to the corporations and to the various municipalities; for while the assessments are made by a state board, the taxes based thereon are paid to the local authorities and not to the State. In the year 1900, when the law first became operative, the assessments on special franchises in the entire State aggregated a little more than \$266,000,000. For the year 1907 the aggregate assessments were over \$555,000,000, of which nearly \$467,000,000 represented assessments of special franchises in New York City.

It is to be hoped that within a very few years the difficult and important questions involved in this new species of taxation will be settled by the courts on a fair and satisfactory basis.

RELATION OF FRANCHISE TAXATION TO SERVICE RATES

BY ALLEN RIPLEY FOOTE

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IN all discussions of the subject of franchise taxation, the precise form of franchise referred to is a grant, made by a state or by a municipality, of a right to exercise the power of eminent domain for the purpose of acquiring a right-of-way, or a grant of a right to use public rights-of-way, for a special purpose and in a special manner not permitted to other users. Such franchises are granted to or are operated by all public service corporations, such as steam railroads, interurban and street railroads, express, telegraph and telephone corporations, and light, heat and power corporations. In granting such franchises the State has, or should reserve, the right to regulate the service rates or tolls that may be charged by such corporations for the services rendered by them to public and private users.

THE PURPOSE TO BE SERVED

Why are franchises granted? Why is the right to regulate rates reserved by the State? Manifestly it is to secure for the use and benefit of the people of a State, or of a municipality, adequate service, such as the corporation to which the franchise is granted is organized to render, of the best possible character and at the lowest possible price. It is obvious that a tax of any kind assessed on the property, franchises or gross earnings of public service corporations must inevitably, to the degree in which such tax may have power to affect rates, tend to defeat the purpose for which franchises are granted and the right to regulate rates is reserved.

Economic efficiency, to result in the lowest economic charge to users of a service, requires the adoption of the policy of no

taxes and correspondingly low rates, instead of the policy of high taxes and correspondingly high rates. The statement that *high taxes and low rates are incompatible* is axiomatic.

FRANCHISE TAXATION AN UNSOUND PROPOSITION

If the purpose of those who advocate franchise taxation is to secure the best possible results for the people from the operation of the franchise granted, their proposition is unsound, because a franchise cannot be taxed without adding the amount of the tax to the cost of the service rendered. In exercising its reserved right to regulate rates, the State must take into consideration this tax addition to cost, as the rates it fixes or approves must cover all costs of ownership and operation and yield a reasonable profit. For this reason a tax on a franchise is not a tax on a corporation — it is a tax on the users of the service it renders. *A franchise tax is paid by users, not by a corporation.* It is a method of plucking feathers from a goose without exciting a perceptible squawk. In fact, by reason of being inadequately informed, or by being misinformed, a franchise tax is a popular demand made by users, or rather by political vote seekers. It is a form of indirect taxation that has no proper place in the economic policy of an intelligent, honest-minded, self-governed people.

FRANCHISE TAXATION IS THE CAUSE OF OVERCAPITALIZATION AND FRAUD

A franchise cannot be taxed without being valued. Its taxable and its commercial value is determined by the capitalized profit, actual or potential, it may enable its owners to earn. To give value to the franchise this profit must be in excess of the reasonable profit all fair-minded persons agree should be earned upon the amount of capital necessarily and actually employed in the business. It is, therefore, a fraudulent profit filched from users through rates that are higher than are necessary to return a reasonable profit on a legitimate investment.

A franchise is worth for capitalization whatever it is valued at for taxation. The proposition to tax a franchise at, say, 3 per cent on the value at which it is assessed for taxation, is

a proposition to take 3 per cent of that value for the benefit of the State and to permit the political and financial speculators, who manipulate state legislatures and municipal councils to secure franchise grants, to pocket 97 per cent by capitalizing the assessed value of the franchise.

When a State declares that a franchise has a taxable value, it declares its intention to exercise its right of rate regulation in a way to enable the corporation owning the franchise to charge rates that will produce a profit on the value so taxed. It incidentally declares that the corporation may issue stock to cover such valuation on the authority of the state-determined value of the franchise. The higher the franchise value is fixed, the greater will be the overcapitalization, the larger will be the state revenue derived from the tax, and the higher will be the rates users must pay in perpetuity to produce the corporation income out of which a reasonable profit can be paid on the capitalized value of the franchise and the tax required by the State. When the day comes, as it surely will, when the people have acquired a correct understanding of this method of public and private financiering and they demand, as they surely will, that taxes and profits on franchise valuations shall cease, the stock will be owned by innocent investors to whom it will have been sold by its original holders, the political and financial speculators who secured the franchise. For examples of the successful manipulation of franchises as described, I refer to the published reports of the investigations being made by the New York Public Service Commissions, and the work of the New York State Board of Tax Commissioners.

In the report of this Board for 1906, the assessed value of all public service franchises in the State is placed at \$427,951,459. Can the people of New York blame the owners of these franchises for anticipating the valuation placed on them by the State and selling stock as a means of placing this enormous value in their own pockets?

Evidence is not wanting, and it is growing clearer and stronger every day, that the time is near at hand when corporations and the State will be brought into agreement regarding sane and safe methods of rate regulation which will result in the fixing of rates to earn only sufficient to pay all legitimate costs of

ownership and operation plus a reasonable profit on a *bona fide* investment. With this agreement will come an irresistible demand for the repeal of all franchise tax laws.

Having reached this conclusion, I may be permitted to consider for a moment the broader question of the relation of taxation to service rates.

THE TAXATION OF PUBLIC SERVICE CORPORATIONS

It is a fact that all taxes and public charges of every kind paid by public service corporations, whether municipal, state, or national, are items of expense and enter into the general statement of the costs of ownership and operation which must be taken into consideration by corporation managers, State Commissioners, or the Interstate Commerce Commission, whenever service rates are reviewed for the purpose of determining their reasonableness. It is also clear, when the system of accounting is sufficiently developed to become uniform for public service corporations of all classes and to produce comparable statistics, properly classified, of all costs of ownership and operation, and of all earnings and receipts of every kind, that a mathematical rule for determining the reasonableness of rates can be devised and given legal effect in statutory law by means of which corporation managers, State Commissions, State Legislatures, the Interstate Commerce Commission, the Congress and all courts, state and federal, can be guided in reaching their conclusions. When such a rule has been formulated and enacted into law, the conclusions of corporation managers will almost invariably be found to be correct by all reviewing commissions and tribunals, and all acts of legislation that do not properly conform to the requirements of the rule (if legislative acts fixing rates are ever again attempted) will be promptly overruled by state and federal supreme courts.

If it is possible to formulate a mathematical rule for the determination of the reasonableness of a rate, it will be found to be far easier to formulate a mathematical rule for determining the reasonableness of a tax which becomes a part of the service rate. That a tax may sustain an obvious and fair relation to the service rate of which it is a part, it must be assessed upon gross earnings, concerning the amount of

which there cannot be two opinions, and not upon property or franchise valuations, upon which there must be, in the nature of things, as many opinions as there are assessors whose duty it is to fix the value of property or of franchises for the purposes of taxation.

One cause of the difference of opinion regarding property and franchise valuations is the widely accepted fallacy that there must be established a comparable relation between the value of the property and franchises of public service corporations and the property of other forms of corporate and individual industries. The organic difference between their purposes, regulation, and the elements in the cost of the services or commodities they sell, renders such comparisons an economic impossibility. The percentage of income paid out for material and labor in keeping rented property in service is very small. The percentage of income from the sale of farm products paid out for labor and material is also small. The percentage of income from the sale of manufactured products paid out for labor and material varies greatly. The cost of some commodities is almost entirely for labor, while of others it is almost entirely for material. The products of public service corporations are services which must be used when and where produced, and which cease to exist when used. The water or power that turns the wheel never returns to turn the wheel again. Over 57 per cent of the gross earnings of public service corporations is paid out for labor. There can be no economic comparison between property used to provide services and property used to produce commodities or rental incomes. These facts should always be held clearly in mind when considering the question of the taxable value of public service corporation property and franchises.

OBJECTIONS TO A GROSS EARNINGS TAX

Objection is made to the adoption of a gross earnings tax to the exclusion of all other forms of taxation, on the ground that the pressure of the tax will be unequal on the net earnings of different corporations, and of the same corporation at different times. This is true. A tax on net earnings is undoubtedly economically more scientific than a tax on gross earnings, but it is not as practical and is far more inquisitorial than a tax on

gross earnings. The relation of a net earnings tax to service rates cannot be as obvious nor as easily determined as a gross earnings tax. Besides this, all public service corporations do not produce net earnings,—some of them produce deficits,—but all of them produce gross earnings. They cannot operate without producing gross earnings.

The objection to a gross earnings tax on the ground of its unequal pressure on net earnings can be overcome in a very simple and practical way. Any system of accounting worthy of the name must disclose the relation between total costs of ownership and operation and gross earnings. A low gross earnings tax may be fixed which all public service corporations must pay, in lieu of all other taxation, whether their accounts show net earnings or not. This would follow the custom of taxing all property whether its use produces an income or not. Having fixed the basic gross earnings tax, a scale for a graduated increase of the tax could be determined by the relation of total costs of ownership and operation to gross earnings, a fraction of a per cent being added to the basic tax for every per cent of variation between costs and earnings. In this way substantial justice can be realized for every public service corporation and at the same time a mathematical rule can be formulated for determining the rate of the tax in any specific case on a basis concerning which there cannot be two intelligent but differing opinions.

ADMINISTRATIVE ADVANTAGES OF A GROSS EARNINGS TAX

A gross earnings tax will produce a large revenue with the least possible machinery and expense for its collection. This may not commend it to politicians who want the largest possible number of places and the greatest possible emoluments for faithful party workers, but should recommend it strongly to the users of the services who, as a final result, must pay the tax through service rates.

GROSS EARNINGS A GROWING BASIS FOR TAXATION

A gross earnings tax will furnish a growing basis for taxation, and, as a result, a growing revenue. This is clearly demonstrated by experience in Ohio. In 1896 the legislature of Ohio

enacted a law levying an excise tax of one half of 1 per cent on the gross earnings of public service corporations. In 1902 it increased this tax to 1 per cent. The enactment of this law made it necessary for the State to require reports from all public service corporations doing business in Ohio, showing the amount of their gross earnings derived from business done within the State. The total gross earnings reported for the year 1896, the year in which the law was enacted, was \$93,309,678. The total valuation of all property in the State, as valued for taxation and shown by the grand duplicate for the year 1896, was \$1,741,028,437. The total gross earnings reported for the year 1906 was \$205,088,338. The total value of all property in the State, as valued for taxation and shown by the grand duplicate for 1906, was \$2,239,786,903. The growth of the gross earnings basis for taxation during the ten years was 119.82 per cent. The growth of the property valuation basis for taxation during the same ten years was only 28.64 per cent. This demonstrates the economic unsoundness of the proposition to retain property valuation instead of adopting gross earnings as an exclusive basis for the taxation of all public service corporations.

CONCLUSION

For the interval of time that must elapse before the economic education of the people will be sufficiently advanced to cause them to discard all forms of indirect taxation, a gross earnings tax, supplemented with proper differentials as described, is earnestly recommended for the taxation of all public service corporations. By applying this tax in lieu of all other forms of taxation, and carefully studying its effect upon service rates, the people will soon learn that a *low tax, or no tax, and low service rates are economic twin sisters.*

GOVERNOR GUILD: We will proceed to the business session.

The first business in order is the report of the Committee on Resolutions, and I will ask your attention to the report, given by the chairman, Mr. Purdy.

MR. PURDY: Your Committee on Resolutions and Conclusions, composed of one member from each State and Province represented, first formed a subcommittee of five. That subcommittee had presented to it various subjects for resolutions, held several sessions, and after very serious and lengthy consideration, framed resolutions in such careful and precise language as would harmonize divergent points of view. To-day those resolutions were submitted to the full committee, and with one verbal change were unanimously approved by the full committee. Should the language chosen appear to be not quite the best, yet the resolution in the main satisfactory, I beg that gentlemen will not lightly change the language for the sake of an improved English style, for the words chosen have just harmonized these divergent opinions.

"RESOLUTIONS

"1. *Resolved*, That a Committee on Finance and Publication be appointed to be charged with the duty of compiling, publishing and distributing to the delegates and to others a record of the proceedings of this Convention;

"Provided, however, that the funds necessary to defray the expense thereof be contributed; and be it

"*Resolved*, That said committee is hereby authorized to receive funds for this purpose."

This resolution was adopted by unanimous vote.

"2. *Inheritance Taxation*

"*Whereas*, The several States are now taxing inheritances with marked success, and need all the revenue that can properly be drawn from this source; and

"*Whereas*, The federal government can readily raise additional revenue, when required, from other sources;

"*Resolved*, That it is the sense of this Conference that inherit-

ance taxes should be reserved wholly for the use of the several States."

This resolution was adopted by unanimous vote.

"3. *State Constitutions*

"*Whereas*, The greatest inequalities have arisen from laws designed to tax all the widely differing classes of property in the same way, and such laws have been ineffective in the production of revenue; and

"*Whereas*, The appropriate taxation of various forms of property is rendered impossible by the restrictions upon the taxing power contained in the constitutions of many of the States;

"*Resolved*, That all state constitutions requiring the same taxation of all property, or otherwise imposing restraints upon the reasonable classification of property, should be amended by the repeal of such restrictive provisions."

This resolution was adopted by unanimous vote.

"4. *Interstate Comity*

"*Whereas*, The principles of international and interstate comity require that the same property should not be taxed by two jurisdictions at the same time, and the laws for the taxation of the transfer of property at death commonly transgress these principles, be it

"*Resolved*, That succession and inheritance tax laws should be so amended that the same property shall not be taxed by two jurisdictions at the death of the owner;

"*Resolved*, That the same principles should be applied in all tax legislation, to the end that no property should be taxed by two state jurisdictions at the same time; and

"*Whereas*, Retaliatory taxation is contrary to interstate comity and is in the nature of interstate war, be it

"*Resolved*, That all retaliatory legislation should be repealed."

This resolution was adopted by unanimous vote.

"5. *Public Debts*

"*Whereas*, The United States Supreme Court truly stated that a tax on public debts is a tax on the power of States, counties and municipalities to borrow money,

"Resolved, That the public debts of all States, counties and municipalities should everywhere be exempted from taxation."

This resolution was adopted by unanimous vote.

"6. Home Rule

"Whereas, The reliance by state government for revenue upon the taxes ordinarily imposed on property as assessed by local officials had produced sectional injustice and jealousy and local inequality; and

"Whereas, The general property tax as a source of state revenue enforces a rigid uniformity which can take no account of actual conditions, be it

"Resolved, That state and local revenue systems should be so far divorced that by general laws the appropriate local governing bodies may be granted certain limited and carefully prescribed powers over the licensing of occupations and the selection of subjects of local taxation and the rate of assessment upon such subject."

MR. FROST (Washington): As a member of the Committee on Resolutions, I reserved the right, when this last resolution was adopted, to express my objection to it, and in expressing my objection, I first wanted to be enlightened upon this subject; but all the gentlemen who have talked upon the proposition of divorcing state from locality for the purposes of taxation, that is, separating the sources of revenue, as is proposed by this solution, took it for granted that that carried with it local option in the matter of taxation. I have not heard the matter discussed from any other viewpoint. In the State of Washington we are proposing to do practically what this resolution would imply, but we do not propose to allow the local authorities any question as to what property should be taxed, and that portion of the resolution I do not think proper. I think we should declare in this resolution that state and local revenue systems should be divorced, but I do not think the resolution should go far enough to say that the local authorities should be given power to select subjects of taxation.

MR. PURDY: If the gentleman from Washington will read the resolution, he will see that the resolution does not so direct. The resolution says, "may be granted." The point is that such

a division should be made, manner of it not prescribed, that it would be possible, if desired, to grant certain limited or prescribed powers over the licensing of occupations and the selection of subjects of local taxation. The gentleman will observe, however, that the resolution does not recite that such powers shall be granted, but that state and local taxation should be so far divorced that such powers "may" be granted.

MR. FROST: Be granted by the state government?

MR. PURDY: If they wished to do it. There is now pending before the people of Missouri, a constitutional amendment, which provides that state and local taxation shall be divorced, the manner not prescribed in the resolution, after 1909; and that thereupon cities may have their charters so amended as to give them powers of local discretion in taxation matters. The mere adoption of the resolution by the people of the State of Missouri will not operate to grant that power; the passage of the resolution will operate to permit the legislature to grant this power, when such divorce has taken place as is contemplated by the resolution.

MR. SUTRO (New York): I must say that the objection made by the gentleman from Washington impresses me as having some force. I think that word "may" might be misconstrued in that relation. It almost sounds as if state and local taxation must be divorced, should be divorced, in order that local officials may have the power to select the objects that should be taxed locally. I think myself it is going a little too far. I think if the words "if deemed expedient" were inserted after the word "may," it would be put much more in the potential case. I move to amend the resolution by inserting after the word "may," the words "if deemed expedient."

MR. PURDY: The amendment is quite acceptable to the chairman of the Committee.

MR. DIXON (North Carolina): I hope the resolution will pass just as it now reads with that amendment, because it is very clear, to the point and entirely noncommittal.

The question now being on the amendment moved by Mr. Sutro of New York, a vote was taken on the motion to amend, Mr. Frost of Washington voting "No." The motion was declared carried.

The question now being on the passage of the resolution as amended, a vote was taken, resulting in the passage of the resolution as amended, only three votes being registered against it. The resolution as amended was read by the chairman as follows:

"Resolved, That state and local revenue systems should be so far divorced that by general laws the appropriate local governing bodies may, if deemed expedient, be granted certain limited and carefully prescribed powers over the licensing of occupations and the selection of subjects of local taxation and the rate of assessment upon such subject."

MR. RUTHERFORD: I am only wishing to express the great appreciation of the work of this Conference by the visitors from the Dominion of Canada. A large number of immensely valuable papers and addresses have been read and will be of great service, not only in the United States of America, but in Canada as well, and I believe they will all help and tend to form public opinion in favor of a just and fair system of taxation. I think we owe a great debt of gratitude to Governor Harris of Ohio in this matter; he has given the official sanction of the head of a great commonwealth to this meeting. It has brought men here under official sanction, and it has given to the proceedings of the Conference an authority which otherwise I am afraid it might not have had, had it been simply an academic meeting. I wish to express in behalf of the delegates from Canada our great appreciation of this service which Governor Harris has rendered, and of the service of this National Conference on Taxation to the public generally, and I wish to express to our friends in the United States and Ohio our acknowledgment of the great courtesy they have extended to us during our visit, and to hope that some day, collectively or individually, all of you will come to Canada to see us. (*Applause.*)

MR. PURDY: I will read the next resolution:

"7. Resolved, That the Conference on State and Local Taxation expresses its profound appreciation of the great service rendered by the Hon. Andrew L. Harris, Governor of the State of Ohio, to all the States, by the part he has taken in calling this Conference and extending to it in various ways his aid and support."

"Resolved, That each and all of us desire to express our thanks for the great kindness extended to us by the Board of Trade for the use of their auditorium room; to the membership of the Columbus Club for their hospitality; to the city of Columbus for the use of the Public Library and to the citizens of Columbus for many kindly acts."

The resolutions were adopted by unanimous vote.

MR. PURDY: I now have the pleasure of the most grateful act that it has been my privilege to perform at this Conference, in moving the adoption of the following resolution:

"Resolved, That we make very grateful acknowledgment to our chairman, Governor Guild of Massachusetts, who has honored us by presiding over our deliberations and who has endeared himself to us all by the punctilious care he has shown in opening all sessions on time, caring for all the troublesome details of the Conference and treating all the delegates and speakers with most delicate and considerate courtesy."

The above resolution was unanimously adopted by rising vote.

MR. CRANDON (Illinois): Mr. Chairman, I wish to move the adoption of this resolution:

"Resolved, That this Conference extend its thanks to the National Tax Association, and especially to the President, Allen Ripley Foote, for calling the Conference and arranging for its accommodation in the city of Columbus."

This resolution is not at all designed to partake of the perfunctory character of a vote of thanks. We fully realize our indebtedness to the Conference, to the city of Columbus and to Mr. Foote, and I am sure we all express our heartfelt gratitude in voting for this resolution, and I hope this Conference will give a rising vote in its adoption.

The resolution was unanimously adopted by rising vote.

GOVERNOR GUILD: National gatherings like this are worthless unless the work is followed up. We have seen corrupt government in municipalities in the United States driven from power by what seemed like a tidal wave of disapproval; then we have seen the organization of good citizenship which brought about that reform dissolve like snow in a January thaw, and then would the same old corrupt government come back into power and the same practices would go on as before.

Now, gentlemen, we have not accomplished everything at this first meeting. It seems to me we have accomplished much. If we had only passed three of those resolutions, we should have accomplished something; we have at least paved the way for a better understanding of taxation, more uniformity of conditions and a better recognition of the common rights of equity and justice that should prevail, not merely between and among the States of the United States, but the nations of North America. (*Applause.*)

MR. SUTRO: It has just occurred to me that before we adjourn and while resolutions are still in order, it would be proper to adopt a resolution to extend the thanks of this Conference to the Press of the United States for the interest it has taken and the reports it has given with regard to this Conference.

GOVERNOR GUILD: Mr. Sutro of New York moves the adoption of a resolution that this Conference hereby extends its thanks to the Press of both nations for the courtesy and attention shown to the deliberations of this Conference.

On vote the resolution was unanimously adopted.

GOVERNOR GUILD: One word more; various votes of thanks have been passed in this Conference. We have all greatly enjoyed these sessions. You see the engine, the machinery; you see the train of cars; you hear the bell and the whistle; but the steam, the motive power, is not always visible, nor the oil that makes the wheels go round so smoothly. There is one gentleman in our assembly to whose winning tact, fair judgment, absolute impartiality and singleness of purpose, untiring zeal and energy, we all owe a very large part of the success of this Conference, the more so, because his work has been inconspicuous — though none the less important on that account — and most thoroughly done. I propose a most hearty vote of thanks to the vice president of the Association, Mr. Lawson Purdy, of New York, and as many as are in favor will so signify by rising.

Unanimously adopted by rising vote. The Conference then adjourned *sine die*.

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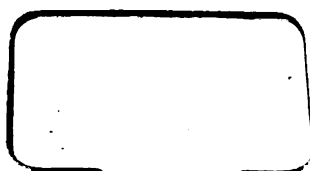


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